

Why A Dollar Collapse Is Inevitable

Alasdair Macleod

We have been here before – twice. The first time was in the late 1920s, which led to the dollar’s devaluation in 1934. And the second was 1966-68, which led to the collapse of the Bretton Woods System. Even though gold is now officially excluded from the monetary system, it does not save the dollar from a third collapse and will still be its yardstick.

This article explains why another collapse is due for the dollar. It describes the errors that led to the two previous episodes, and the lessons from them relevant to understanding the position today. And just because gold is no longer officially money, it will not stop the collapse of the dollar, measured in gold, again.

General de Gaulle made himself very unpopular with the international monetary establishment by holding the press conference from which the opening quote was taken. Yet, his prophecy, that the gold exchange standard of Bretton Woods would end in tears unless its shortcomings were addressed by a return to a gold standard, turned out to be correct shortly after. What the establishment did not like was the bald implication that it was wrong, and that the correct thing to do was to reinstate the gold standard. Plus ça change, as he might say if he was still with us.

Those of us who argue the case for a new gold standard, and not some sort of half-way house such as a gold exchange standard to address the obvious failings of the current monetary system, are in a similar position today. The first task is that which faced General de Gaulle and Jacques Rueff, his economic advisor, which is to explain the difference between the two. It is now forty-seven years since all forms of monetary gold were banished by the monetary authorities, and today few people in finance understand its virtues.

Furthermore, in the main, historians educated as Keynesians and monetarists do not understand the economic history of money, let alone the difference between a gold standard and a gold-exchange standard. These similar sounding monetary systems must be defined and the differences between them noted, for anyone to have the slimmest chance of understanding this vital subject, and its relevance to the situation today.

Defining the role of gold

To modern financial commentators, there is little or no significant difference between a gold standard and a gold exchange standard. Keynes’s famous quip, that the gold standard was a barbarous relic, was made in his *Tract on Monetary Reform*, published in 1923, before the gold exchange standard really got going, yet it is quoted as often as not indiscriminately in the context of the latter.

Yet, they are as different as chalk and cheese. The gold exchange standard evolved in the 1920s as America and Britain went to the aid of European countries, struggling in the wake of the Great War. It allowed the expansion of national currencies under the guise of them being as good as gold. It was not. In modern terms, it was as different as paper gold futures are to the possession of physical gold today.

A gold standard is commodity money, where gold is money, and monetary units are defined as a certain fixed fineness and weight of gold.

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Has The Subprime Auto Bubble Burst?

Peter Schiff

It looks like the subprime auto loan bubble has popped.

Last year, we reported that [the auto industry’s check engine light was on.](#) Now it looks like the thing is totally breaking down. Small subprime auto lenders are starting to go belly-up due to increasing losses and defaults. As *ZeroHedge* noted, “we all know what comes next: the larger companies go bust, inciting real capitulation.”

[Bloomberg recently reported](#) that not only are subprime auto lenders facing tough business conditions, there are also allegations of fraud and under-reporting of losses.

Growing numbers of small subprime auto lenders are closing or shutting down after

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This Really Is The Everything Bubble: Even Subprime Mortgage Bonds Are Back

John Rubino

Record student loan balances? Check. Trillion dollar credit card debt? Check. Six tech stocks dominating the Nasdaq? Check. Subprime auto loans at record levels? Check.

All that's missing is subprime mortgages and we'd have every bubble base covered. Oh wait, those are back too, just under a different name:

Subprime mortgages make a comeback— with a new name and soaring demand

They were blamed for the biggest financial disaster in a century. Subprime mortgages – home loans to borrowers with sketchy credit who put little to no skin in the game. Following the epic housing crash, they disappeared, due to strong, new regulation, and zero demand from investors who were badly burned. Barely a decade later, they're coming back with a new name – nonprime – and, so far, some new standards.

California-based Carrington Mortgage Services, a midsized lender, just announced an expansion into the space, offering loans to borrowers, “with less-than-perfect credit.” Carrington will originate and service the loans, but it will also securitize them for sale to investors.

“We believe there is actually a market today in the secondary market for people who want to buy nonprime loans that have been properly underwritten,” said Rick Sharga, executive vice president of Carrington Mortgage Holdings. “We’re not going back to the bad old days of ninja lending, when people with no jobs, no income, and no assets were getting loans.”

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loan losses and slim margins spur banks and private equity owners to cut off funding. Summit Financial Corp., a Plantation, Florida-based subprime car finance company, filed for bankruptcy late last month after lenders including Bank of America Corp. said it had misreported losses from soured loans. And a creditor to Spring Tree Lending, an Atlanta-based subprime auto lender, filed to force the company into bankruptcy last week, after a separate group of investors accused the company of fraud. Private equity-backed Pelican Auto Finance, which specialized in ‘deep subprime’ borrowers, finished winding down last month after seeing its profit margins shrink.”

We’ve heard this song and seen this dance before. As *Bloomberg* noted, the pain among small auto lenders “parallels with the subprime mortgage crisis last decade, when the demise of finance companies like Ownit Mortgage and Sebring Capital Partners were a harbinger that bigger losses for the financial system were coming.”

The common denominator here: rising interest rates. Easy money pumped up both the housing and auto loan bubble. When the Fed takes away the punchbowl, bubbles burst.

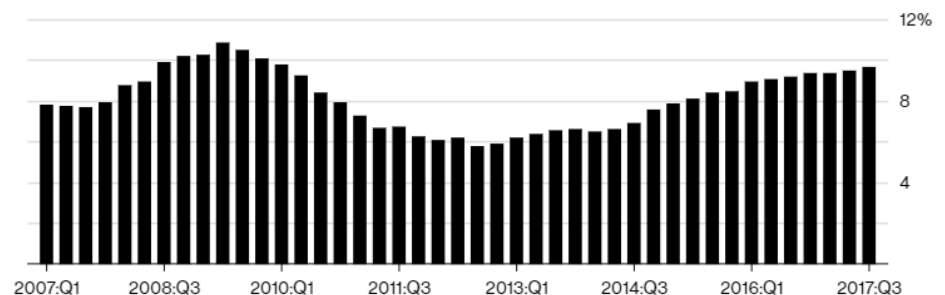
Chris Gillock works as an analyst for Colonnade Advisors, focusing on subprime auto investments. His description of the auto loan industry sounds a lot like mortgage lending back in the years leading up to the housing bust.

There’s been a lot of generosity and not a lot of discretion on the part of lenders and investors. There’s going to be more capitulation.”

Auto loans to subprime borrowers have hit delinquency rates not seen since 2010. The number of borrowers behind on payments has been increasing steadily since 2012. In the third quarter of 2017, nearly 10% of auto loans extended to consumers with a credit score of less than 620 were 90 days or more behind.

Non-bank lenders' subprime auto loans are going bad at the highest rate since 2010

■ 90+ Day Delinquent Auto Finance Company Loans to <620 Credit Score Borrowers



Source: New York Fed Consumer Credit Panel/Equifax

In another bad sign for the auto market, subprime borrowers have gone missing from auto showrooms. According to Bloomberg, rising interest rates and rapidly increasing vehicle prices are squeezing consumers with shaky credit and tight budgets out of the market. Even the most creditworthy consumers aren't showing up to dealerships.

In the first two months of this year, sales were flat among the highest-rated borrowers, while deliveries to those with subprime scores slumped 9%, according to J.D. Power. The researcher's data highlights what's happening beneath the surface of a US auto market in its second year of decline after a historic run of gains. Automakers probably will report sales in March slowed to the most sluggish pace since Hurricane Harvey ravaged dealerships across the Texas Gulf Coast in August, according to Bloomberg's survey of analyst estimates.”

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The monetary authority is obliged by law to exchange without restriction gold against monetary units and vice-versa, and there are no restrictions on the ownership and movement of gold.

Under a gold exchange standard, the only holder of monetary gold is the issuer of the domestic monetary unit as a substitute for gold. The monetary authority undertakes to maintain the relationship between the substitute and gold at a fixed rate. Only money substitutes (bank notes and token coins – gold being the money) circulate in the domestic economy. The monetary authority exchanges all imports of monetary gold and foreign currency into money substitutes for domestic circulation at the fixed gold exchange rate. The monetary authority holds any foreign exchange which is also convertible into gold on a gold exchange standard at a fixed parity, and treats it to all extents and purposes as if it is gold.

The essential difference between a gold standard and a gold exchange standard is that with the latter, the monetary authority has added flexibility to expand the quantity of money substitutes in circulation without having to buy gold. A gold standard may start, for example, with 50% gold and 50% government bonds backing for money units, but all further issues of monetary units will require the monetary authority to purchase gold to fully cover them. This was the monetary regime in Britain and many other countries before the First World War.

As stated above, gold exchange standards evolved after the First World War, in the early 1920s. It was the taking in of foreign currencies, also on gold exchange standards themselves, and booking them as if they were the equivalent of gold, that allowed central banks to expand the quantity of monetary units domestically. To understand how this operated in practice requires us to work through an example between two countries on gold exchange standards. We will take the entirely hypothetical example of two countries, America and Italy, both of which have monetary gold in their reserves and operate on a gold exchange standard.

America lends Italy dollars by crediting its central bank's account at the Fed with the dollars loaned. But while ownership has changed to Italy, dollars never leave America. And dollars, when drawn down by the Banca d'Italia are recycled into America's banking system.

The economic sacrifice to America of lending money to Italy is therefore zero. America has simply created a loan out of its own currency, and in the process increased the quantity of dollars in circulation. And because in practice Italy does not encash dollars for gold, America expects to preserve its gold reserves.

Meanwhile, The Banca d'Italia has expanded its balance sheet by the inclusion of America's dollar loan to it as a liability, and the dollars themselves as an asset regarded as the equivalent of gold. Because dollars are not permitted to circulate in Italy's domestic economy, they can be used by Banca d'Italia, either to settle other foreign obligations, or as a gold substitute to back the issue of further lira. Meanwhile, the Banca d'Italia's dollars are reinvested in US Treasuries, which give a yield. Banca d'Italia has little incentive to exchange its dollars for physical gold, because gold yields nothing and is costly to store.

If Banca d'Italia uses dollars to discharge a foreign obligation with another country, that third party will also end up investing the dollars gained in US Treasuries, assuming it also prefers yielding assets to physical gold. Alternatively, if the dollars are used by the Banca d'Italia to back an increase in the quantity of lira or to subscribe for government debt, the effect in the domestic Italian economy is an inflation of prices.

Therefore, the effect of a gold exchange standard is the opposite of a gold standard. A gold standard puts the requirements for the quantity of money in circulation entirely in the hands of the market, to which the central bank mechanically responds. A gold exchange standard allows a lending central bank to inflate its money supply through inward investment, and a borrowing central bank to inflate its money supply on the presumption the monetary substitutes borrowed to back it are monetary units of gold.

The gold exchange standard in the 1920s

After the First World War, both sterling and dollars were made available under the Dawes Plan of 1924, which provided non-domestic capital for Germany after her hyperinflation. France suffered a currency crisis in July 1926, which was successfully dealt with by the Poincaré government through raising taxes.

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THE Acronym Of 2008 Is Sounding Another Alarm

Michael Pento

LIBOR, or the London Interbank Offered Rate, was the most important acronym most investors never heard of before 2008. However, it quickly became the most critical variable in markets leading up to the Great Recession.

What has now become clear is that we haven't learned any lessons from the financial crisis except how to accumulate more debt and to artificially control markets more extensively. And, to conveniently try to sweep under the rug the very same warning signs that forebode the day of reckoning just over a decade ago.

Today, the main stream financial media is obsessed with inane Congressional hearings surrounding Facebook—as if it were a surprise to users that the company's privacy policy is to invade it—rather than talking about the more salient issues...like LIBOR.

In layman's terms, LIBOR is the average interest rate required by leading banks in London to lend to one another. It originated in 1969 when a Greek banker by the name of Minos Zombanakis, arranged an \$80 million syndicated loan from Manufacturers Hanover to the Shah of Iran. Zombanakis constructed the loan using reported funding costs derived from a group of reference banks in London. Other banks began tying debt to this rate, and by the mid-1980s the British Bankers' Association took control of this new rate that we now refer to as LIBOR. Today, the banks that encompass the LIBOR panel are the most significant and creditworthy in London.

LIBOR performs two major purposes for today's markets. First, it serves as a reference rate used to establish the terms of financial instruments such as short-term floating rate financial contracts like swaps and futures. It also serves as a benchmark rate—a comparative performance measure used for investment returns.

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Americans simply can't afford to buy vehicles. ZeroHedge compiled a number of statistics that reveal just how unhealthy the automobile market in the US has become.

- The average price for a new vehicle is at a record high \$31,099.
- The average price of a used car is a record high \$19, 589.
- The average monthly payment for new and used cars has hit a record high of \$515 per month.
- The average auto loan has hit a record high of 69 months.

Notice the theme here — record high.

ZeroHedge summed it all up.

Cheap credit leads to easy lending conditions, and record prices as everyone floods into the market with lenders hardly discriminating who they give money to.”

And then the bubble pops.

The collapse of the subprime auto industry probably won't have the same impact on the economy as the housing crash did in 2008.

The industry isn't as big in terms of dollars. But what's going on in the auto industry is indicative of broader trends in the US economy. It's not the only bubble.

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Peter Schiff
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Sharga said Carrington will manually underwrite each loan, assessing the individual risks. But it will allow its borrowers to have FICO credit scores as low as 500. The current average for agency-backed mortgages is in the mid-700s. Borrowers can take out loans of up to \$1.5 million on single-family homes, townhomes and condominiums. They can also do cash-out refinances, where borrowers tap extra equity in their homes, up to \$500,000. Recent credit events, like a foreclosure, bankruptcy or a history of late payments are acceptable.

All loans, however, will not be the same for all borrowers. If a borrower is higher risk, a higher down payment will be required, and the interest rate will likely be higher.

“What we're talking about is underwriting that goes back to common sense sort of practices. If you have risk, you offset risk somewhere else,” added Sharga, while touting, “We probably are going to have the widest range of products for people with challenging credit in the marketplace.”

Carrington is not alone in the space. Angel Oak began offering and securitizing nonprime mortgages two years ago and has done six nonprime securitizations so far. It recently finalized its biggest securitization yet — \$329 million, comprising 905 mortgages with an average amount of about \$363,000. Just more than 80 percent of the loans are nonprime.

Investors in Angel Oak's nonprime securitizations are, “a who's who of Wall Street,” according to company representatives, citing hedge funds and insurance companies. Angel Oak's securitizations now total \$1.3 billion in mortgage debt.

Angel Oak, along with Caliber Home Loans, have been the main players in the space, securitizing relatively few loans. That is clearly about to change in a big way, as demand is rising.

“We believe that more competition is positive for the marketplace because there is strong enough demand for the product to support multiple originators,” said Lauren Hedvat, managing director, capital markets at Angel Oak. “Additionally, the more competitors there are, the wider the footprint becomes, which should open the door for more potential borrowers.”

Big banks are also getting in the game, both investing in the securities and funding the lenders, according to Sharga.

“It's large financial institutions. A lot of people with private capital sitting on the sidelines, who are very interested in this market and believe that as long as the risks are managed well, and companies like ours are particularly good at managing credit risk, that it's a good investment opportunity,” he said.

So today's subprime mortgages are being written with lots of common sense safeguards. But demand for the resulting bonds is soaring and lots of new players, big and small, are getting into the game. Wonder what that means for underwriting standards going forward...

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Courtesy of <https://dollarcollapse.com>

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The Bank of France was then enabled to borrow dollars and sterling and to issue francs and subscribe for government debt.

To summarise, these loans bolstered the balance sheets of the Reichsbank and the Bank of France, which invested the sterling and dollars borrowed in gilts and Treasuries respectively. If instead France and Germany had taken gold under the gold exchange provisions, they would have had an asset with no yield, though France did opt increasingly for some gold towards the end of the decade and beyond – by December 1932 she had accumulated 3,257 tonnes. So, by lending their monetary units, the creditor nations achieved finance for their own governments, as well as providing capital for foreign central banks. It was seen to be a win-win for all the central banks involved.

The accumulation of dollars in foreign hands from 1922 onwards accompanied and fuelled bank credit expansion in the US. This gave the roaring twenties an inflationary impetus, dramatically reflected in its stock market bubble. However, the increasing quantity of dollars in foreign ownership became an accident waiting to happen. There had been a mild thirteen-month recession from October 1926 to November 1927, after which the stock market boomed. The Fed was compelled to reverse earlier interest rate cuts and increased the discount rate from 3 ½% to 5% by July 1928.

French investors began to repatriate capital en masse, and the Bank of France's gold reserves rocketed from 711 tonnes in 1926 to 2,099 tonnes by 1930. The gold exchange standard had spectacularly failed, and redemption of dollars for gold, being deflationary, exacerbated the Wall Street Crash. It certainly rhymed with Robert Triffin's dilemma: the export of dollars into foreign ownership was monetary magic, until it reversed at the first sign of trouble.

The gold exchange standard of Bretton Woods

In 1944, the monetary panjandrums of the day, led by Harry Dexter-White for the US and Lord Keynes for the UK, designed the post-war gold exchange standard of Bretton Woods. No doubt, Dexter-White fully understood the advantage to the US of forcing all countries to accept dollars with a yield, or gold with none. When American payments abroad exceeded receipts, the difference was generally reflected in dollars issued to foreign central banks, kept on deposit in New York, or invested in US Treasuries.

Throughout the 'fifties, America recorded a surplus on goods and services, which declined as European manufacturing recovered. But other factors, such as investment abroad and the Korean war resulted in an overall balance of payments deficit totalling \$21.41bn, the equivalent of 19,024 tonnes of gold at \$35 per ounce. However, US gold reserves declined only 4,457 tonnes between 1950 and 1960, which tells us that the balance was indeed invested in US bank deposits and US Government notes and bonds.

The respective figures for the 1960s were total payment deficits of \$32bn, the equivalent of 28,437 tonnes of gold, and an actual decline in gold reserves of 5,283 tonnes. The accelerating increase of foreign ownership of dollars over these two decades meant the world, ex-America, was awash with dollars by the mid-1960s. By the end of that decade, America's gold reserves had declined from 20,279.3 tonnes in 1950, two-thirds of the world's monetary gold, to 10,538.7 tonnes, 29% of the world's monetary gold in 1970.

The effect was to remove trade settlement disciplines on net importing nations, and to cause inflation in net exporting nations, the opposite of the disciplines of a pre-WW1 gold standard on global trade. It was this effect that was central to the second Triffin dilemma, whereby dollars became wildly over-valued in gold terms through their excessive issuance.

In the mid-sixties, Washington became increasingly alarmed that foreigners weren't playing by the assumed rule that they should take dollars and not redeem them for gold. By then, France and Germany between them had increased their gold holdings from 487.1 tonnes in 1948 to 7,089 tonnes at the time of de Gaulle's press conference. General de Gaulle's press conference, from which this article's opening quote is taken, had touched some very raw nerves.

It was clear that the dollar, with the overhang of foreign ownership, had become horribly overvalued, and so should have been devalued, perhaps to over \$50 or \$60 per ounce, for a gold peg to stick. A devaluation of this magnitude might have been sufficient at that time to stem the outflow of gold.

Both Washington and American public opinion were set strongly against any devaluation. Instead, the London gold pool, designed to ensure the major central banks supported the Bretton Woods System, collapsed in 1968, when France withdrew from it. A dollar devaluation to \$42.2222 shortly after was simply not enough, and in 1971 President Nixon suspended the Bretton Woods System, and the new regime of floating exchange rates that is still with us to this day began.

The situation today

Following the Nixon shock, official monetary policy towards gold was to ignore it, and to persuade other central banks and financial markets it was irrelevant to the modern monetary system. To this day, the Fed still books the gold note from the Treasury at \$42.2222 per ounce, even though the price has risen to over \$1300.

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Common sense would tell you that an increase in the LIBOR implies that those top banks comprising the LIBOR panel believe that lending to their fellow financial institutions is becoming riskier; with a significant spike signaling the possibility of economic instability. LIBOR rang an ear-piercing warning bell at the onset of the 2008 financial crisis. Before mid-2007, LIBOR trended with other short-term interest rates such as Treasury yields and the Overnight Index Swap (OIS) rate. But in August 2007, that relationship began to break, signaling the start of liquidity fears that drove the 3-month USD LIBOR up to 5.62%, from its average of 5.36%. During the same period, the overnight Fed Fund's policy target rate for the Federal Reserve remained stable. Therefore, the spread between where traders believed the Fed Funds Rate would be and the rate banks would lend unsecured funds to each other started to blow out.

Ted-Spread One Year Chart



Source: <http://www.macrotrends.net/1447/ted-spread-historical-chart>>TED Spread - Historical Chart

The LIBOR-OIS spread (the difference between LIBOR and OIS) continued to rise as concerns about bank liquidity and credit worthiness compelled interbank lenders to pare back funding and demand even higher rates. This spread, a barometer of the health of the banking system, averaged less than 10 basis points from 2005 to mid-2007, but ballooned to 360 bps following the Lehman Brothers bankruptcy.

LIBOR has once again started to rise. During the last two and a half years it increased from 0.3%, to 2.36%; and the pace of that increase has recently picked up steam. It jumped nearly a full percentage point in the last six months--outpacing the moves of the Federal Reserve. One reason is the deluge of short-term Treasury offerings displacing demand for short-term commercial paper, forcing companies to offer higher rates for their short-duration financing. Another explanation for the recent spike is the repatriation of foreign earnings derived by the recent tax law changes.

Regardless of the reasons surrounding LIBOR's recent spike, its influence in dictating interest rates on roughly \$370 trillion in dollar-based financial contracts globally, from corporate loans to home mortgages, makes it extremely painful for the borrowers on the other end. Its recent jump increased all adjustable rate mortgages whose rate is based off LIBOR. In addition to adjustable rate mortgages and mortgages that have an ARM component, student loans, auto loans and credit cards, are also tied to LIBOR. Most importantly, the LIBOR-OIS spread, which proved to be the canary in the coal mine during the last financial crisis, has just hit its highest level since 2009.

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We can simplistically value the dollar in terms of gold, which is certainly a valid, perhaps the most valid approach. But to merely conclude that the dollar has collapsed since 1971, while true, side-steps an analysis that points to the risk that even today's value may still be too high. Furthermore, with the dollar acting as the world's reserve currency, all other fiat currencies, which are priced with reference to it rather than gold, are to a greater or lesser extent in the same boat.

Taking a cue from our analysis of the workings of cross-border monetary flows, which allows America to have its privilege of foreigners financing its deficits, we can estimate the approximate extent of the accumulated imbalances that could lead to the dollar's collapse.

We know that the US balance of payments deteriorated from 1992 onwards, though those figures did not include military spending abroad, which has been a significant and unrecorded addition to dollars both in cash circulation outside America, and also to estimates of the balance of payments. Official balance of payments figures are therefore understated and have been for at least a quarter of a century.

More recently, from September 2008 the Fed began expanding its balance sheet by policies designed to increase commercial bank reserves, as a response to the financial crisis. That August, they were \$10.5bn, increased to \$67.5bn the following month, and peaked at \$2,786.9bn in August 2014, since when there has been a modest decline. From our analysis of the run-ups to the two previous dollar crises, we know we should try to estimate how much of the increase was effectively funded from abroad. Treasury TIC Data gives us a fairly good steer to what extent this has happened. We find that between those dates, (August 2008 – August 2014) foreign ownership of dollars increased by \$6,237.7bn, over twice as much as the increase in the Fed's record of commercial bank reserves.

This is Triffin at its most fast and furious. Since then, foreign ownership of dollars has increased a further \$2,142.4bn to a record \$18,694.1, even though bank reserves declined by \$572bn. In other words, the accumulation of dollars in foreign hands now stands at over 95% of US GDP. Another way of looking at it is to assess the market values of US securities held by foreigners and relate that to GDP, though this information is less timely. This is shown in the following chart.

The build-up of foreign investment in America, in large measure the counterpart of dollar loans to foreigners, has been remarkable. At the time of the dot-com bubble, it had jumped to 35% of GDP, from less than 20% in the nineties and considerably less before. At over 90% of GDP in recent years, there can be no doubt that the next financial event, whether it be derived from a rise in interest rates or a general weakness in the dollar, can be expected to trigger a substantial flight out of the dollar.

The pricing of financial assets, and today's extraordinarily low interest rates indicate that a flight from the dollar is the last thing expected in financial markets. If they were still alive, de Gaulle and his economic advisor, Jacques Rueff, would be instructing the ECB, as successor to the Bank of France, to dump all dollars for gold immediately. And probably to dump all other foreign fiat currencies for gold as well. However, today, it is likely that other actors will blow the whistle on the dollar, such as the Chinese, and the Russians.

For it is clear that when the over-valuation of the dollar is corrected, the downside of a dollar collapse is far greater than it was in the early-thirties or the early-seventies. All other fiat currencies take their value from the dollar, not gold. So, the destabilising forces on the dollar, the other unexpected side of Triffin's dilemma, could take down the whole fiat complex as well.

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Is Bitcoin A Substitute For Gold?

Arkadiusz Sieron

John Maynard Keynes once famously called gold the "barbarous relic". The emergence of the cryptocurrencies seems to validate that thesis. Will gold survive in the digital era?

Bitcoin as Digital Gold

Let's face it. **Bitcoin** and gold are similar. Both assets are rare and their supply is limited (it cannot be increased at will by politicians or central bankers). Actually, Bitcoin was conceived as the digital gold from the very beginning – the process of generating bitcoins is called "mining". And both Bitcoin (and cryptocurrencies in general) and gold are not government issued media of exchange – instead, both are alternatives to **fiat currencies**.

According to Aswath Damodaran, a valuation guru, one scenario for Bitcoin is that it will become "gold for Millennials", i.e. it will take the role that gold has fulfilled for hundreds of years – a **safe-haven** asset for people who don't trust governments & central banks and their currencies.

But There Are Important Differences

Bitcoin's parabolic rise at the end of 2017 prompted some analysts to claim that cryptocurrencies may replace gold. They forgot that Damodaran's vision was only a one of possible scenarios for Bitcoin's future. And they neglected several distinctions between gold and Bitcoin. The **World Gold Council** has recently published an **investment update**, arguing that cryptocurrencies are no substitute for gold. Their reasons are that gold:

- is less volatile;
- has a more liquid market;
- trades in an established regulatory framework;
- has a well understood role in an investment portfolio;
- has little overlap with cryptocurrencies on many sources of demand and supply

Bitcoin vs. Gold – Volatility

The Bitcoin's enormous volatility is perhaps the biggest obstacle to replace gold. One function of money is to be a store of value such as the yellow metal – as Bitcoin moves, on average, 5 percent each day,

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it hardly serves as a viable medium of exchange. Actually, cryptocurrencies are much more held and used as a speculative investment rather than medium of exchange used for transactions. Gold is not money anymore, but it is definitely used as an **inflation hedge** and a store of value.

Bitcoin vs. Gold – Liquidity

Another important issue is market liquidity. Bitcoin trades, on average, \$2 billion a day, which is less than 1 percent of the total gold market that trades approximately \$250 billion a day. The modest Bitcoin's liquidity is partially responsible for its huge volatility. We know that Bitcoin is still young, but the gold's established role as a monetary asset will be very difficult to dethrone. People have a status quo bias – and there are network effects in operation. Actually, as there are currently over 1,400 cryptocurrencies available, the future of Bitcoin is under question – it has “first-mover advantage”, but we cannot exclude that it would be replaced itself by better cryptocurrency.

Conclusions

We often disagree with the World Gold Council, as it has a clear **bullish** bias toward gold. The shiny metal and Bitcoin have some similarities, but there are not substitutes, at least not perfect. It's not that we don't like cryptocurrencies – we keep our fingers crossed for all alternatives to the government-sponsored fiat money (especially that blockchain technology looks very promising). But we are not blind to obvious differences. Gold has a long history of being monetary asset behind it and the gold market is well established, very liquid and relatively stable. Meanwhile, the cryptocurrency market is young, with small liquidity and high volatility. Investors buy Bitcoin and other alt-coins not as safe-havens, but rather as speculative vehicles. Hence, contrary to some commentators, the gold prices shouldn't be affected by rallies and downturns in cryptocurrencies. Stay tuned!

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www.sunshineprofits.com

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LIBOR provides an essential read to investors about the health of the banking system. It allows them to decipher the risks that exist in the marketplace. But despite LIBOR's role as a Market Oracle, regulators around the globe are working on a replacement because they believe its key market participants can too easily manipulate it.

The scandal that broke in the summer of 2012 arose when it was exposed that banks were falsely manipulating rates in both directions to profit from trades, or to give the illusion that they were more creditworthy.

In the United States, regulators are seeking to replace LIBOR with another acronym SOFR, or the Secured Overnight Financing Rate. A rate based on repurchase agreements--overnight loans collateralized by Treasury securities.

Where SOFR relies technically on a broader swath of market participants and is less prone to manipulation, its collateralization to the U.S. Treasury market ensures that it will no longer provide the vulnerability necessary to predict market risk.

The transition away from LIBOR is likely to be a long one due to the necessity to alter millions of legal contracts tied to this rate. But what should concern bankers and market participants more than the cumbersome legality involved in replacing LIBOR is the loss of this essential free-market indicator.

LIBOR will move out of the hands of sophisticated market participants who are risking the health of their bank when they determine this lending rate and remand it into arms of the U.S. government and the Federal Reserve, which may leave banks and investors fewer warning signs and less options to protect themselves when the next financial crisis hits.

The truth is governments have complete disdain for markets and are seeking to replace them with increasing alacrity. Governments and Central Banks are nearly always on the wrong side of the economy because they choose to ignore the signals that can be derived from whatever is left from the free market. This is why the Fed kept interest rates at near 0% for eight years when the economy was no longer on life support and is now raising rates while LIBOR is foreboding an economic slowdown. And this adds to the reasons why the next and even Greater Recession lies just around the corner.

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