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# Booms, Busts and Monetary Policy

September 26, 2011

Nathan Lewis

Kiku Capital Management LLC

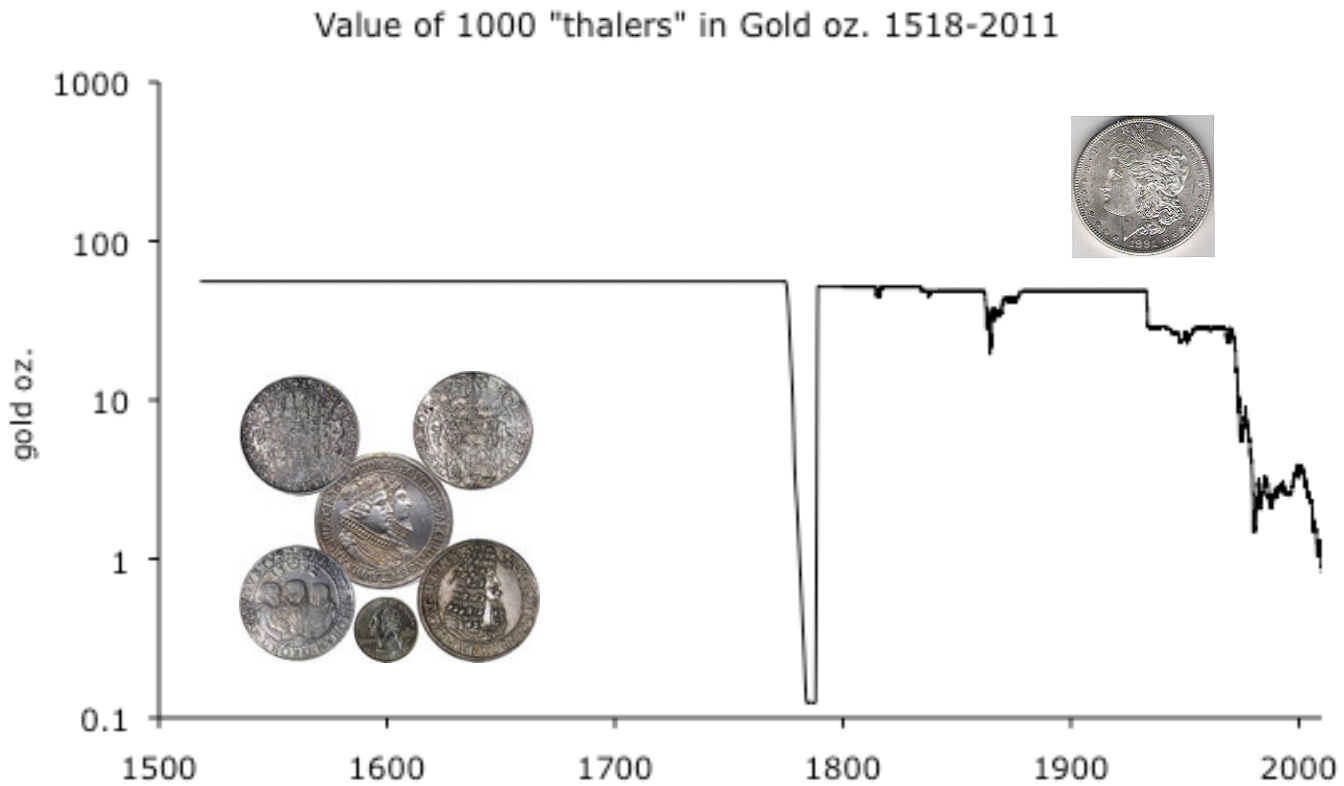
*Gold: the Once and Future Money* (2007)

[www.newworldeconomics.com](http://www.newworldeconomics.com)



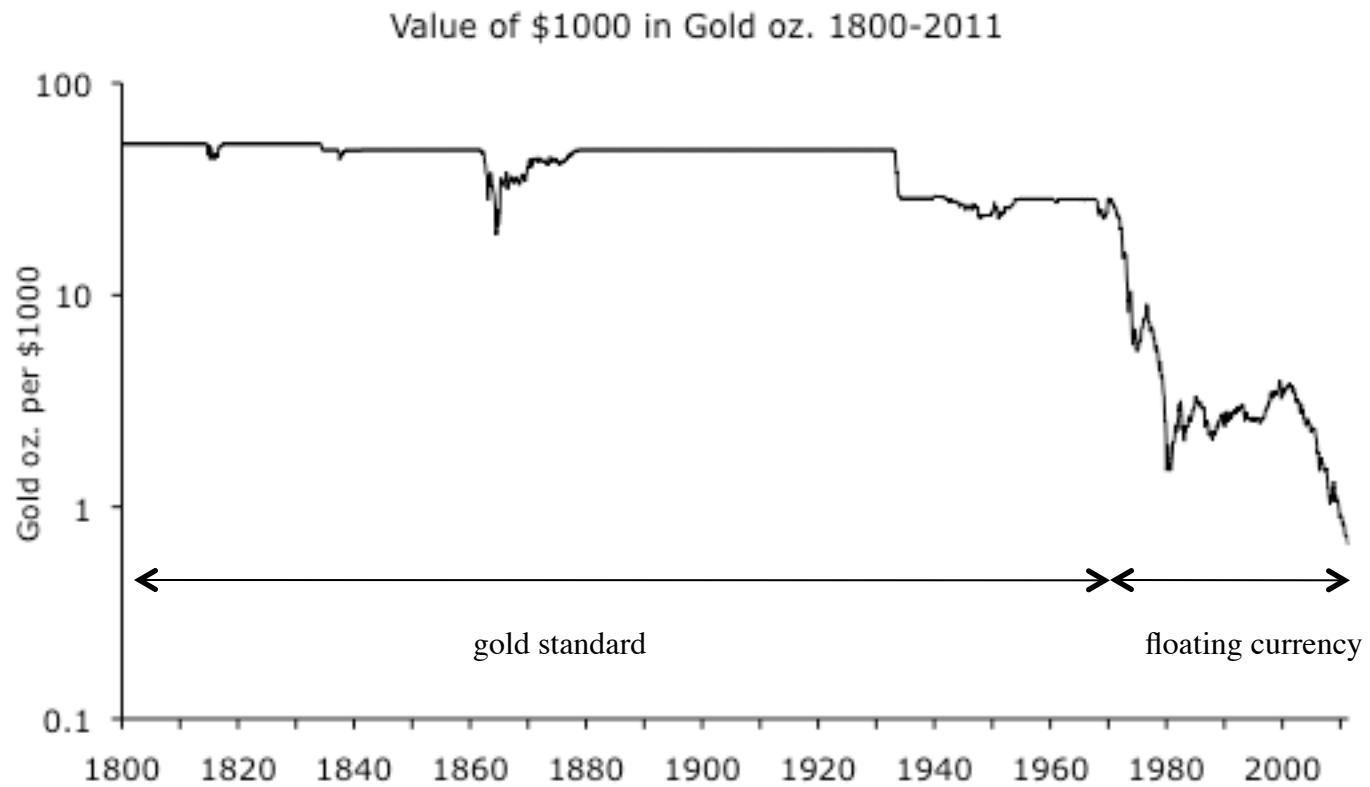
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The European tradition of the “thaler” goes back 500 years. The Austrian “thaler,” the Spanish “dollar,” and the U.S. dollar were all basically identical silver coins (about 29 grams of silver).



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From 1789 to 1971, the U.S. used a gold standard system. There was one permanent devaluation in 1933.

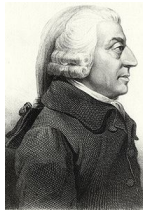


# Two Monetary Paradigms

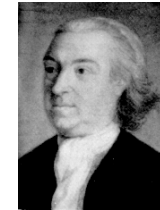
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## Classical Paradigm “Hard Money”

- “Rule of Law”
- Stable currency value is goal.
- Avoid government manipulation.
- Gold link enables stable money.
- Unstable money causes problems
- Leave credit up to the bankers.
- Interest rates left to market.
- Fixed exchange rates are good.
- “You can’t devalue yourself to prosperity.”



Adam Smith vs. James Denham Steuart

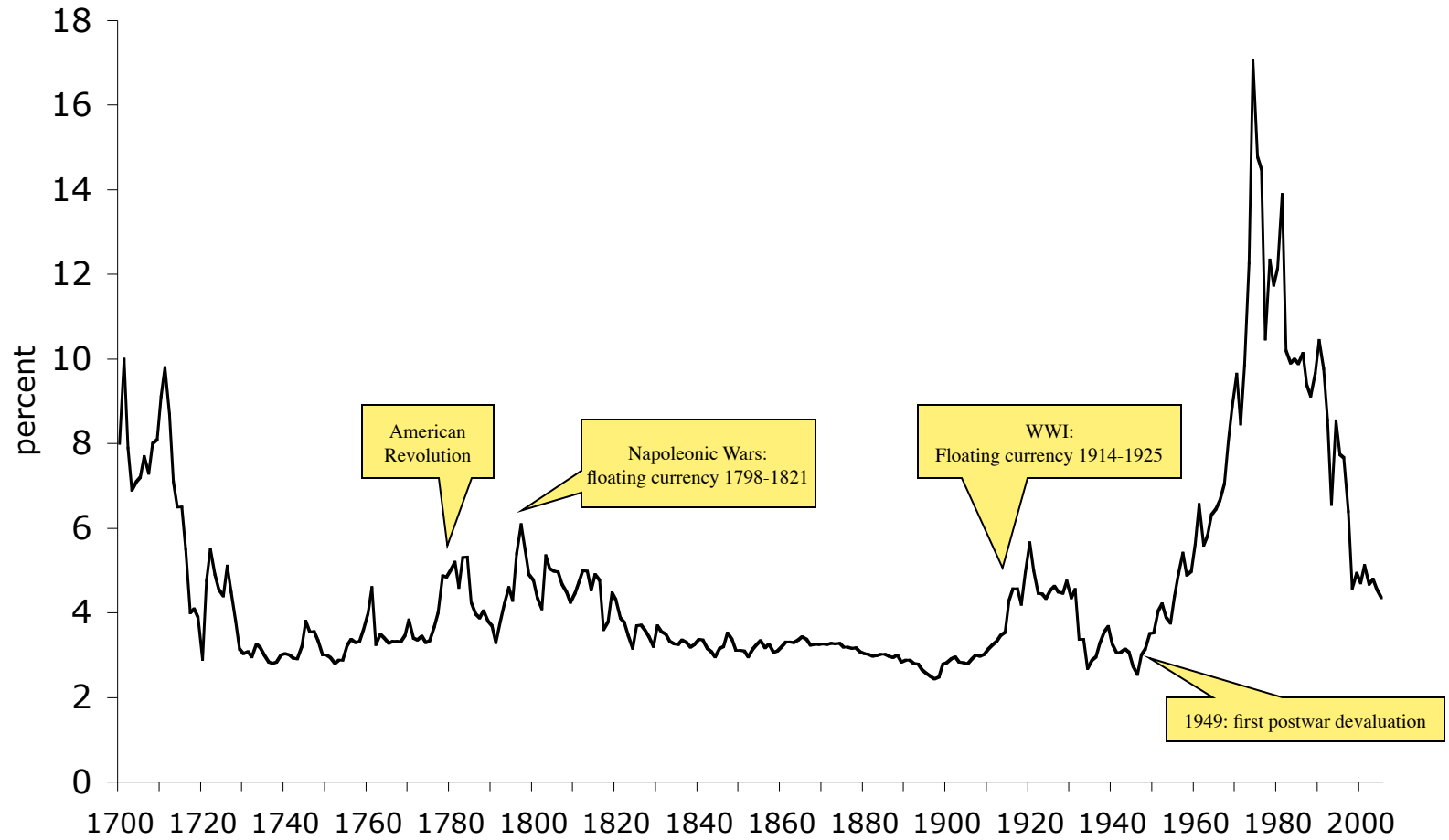


## Mercantilist Paradigm “Soft Money”

- “Rule of Man”
- “Full employment” is goal.
- Constant government “management.”
- Gold link prevents management.
- Money manipulation solves problems.
- Manipulate credit for macro effect.
- Interest rates managed.
- Floating currencies allow “adjustment.”
- “In the long run, we’re all dead.”

*We are in a Mercantilist paradigm today!*

Britain: Yield on 2.5% Consol Bond 1700-2005



## Think of things in “1922 dollars”

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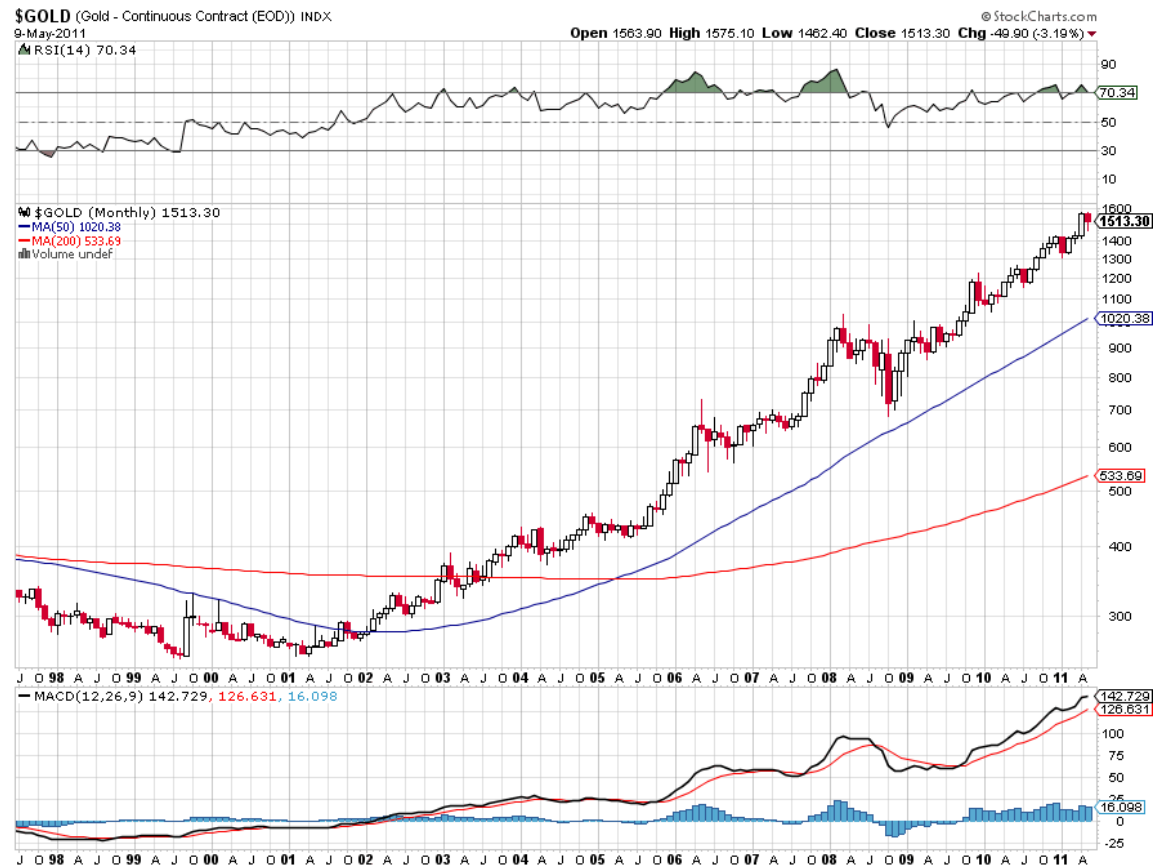


80x

1922 \$20 double eagle  
0.97 oz. of gold

1854 \$20 double eagle  
0.97 oz. of gold

We are now in a new era of declining currency value.



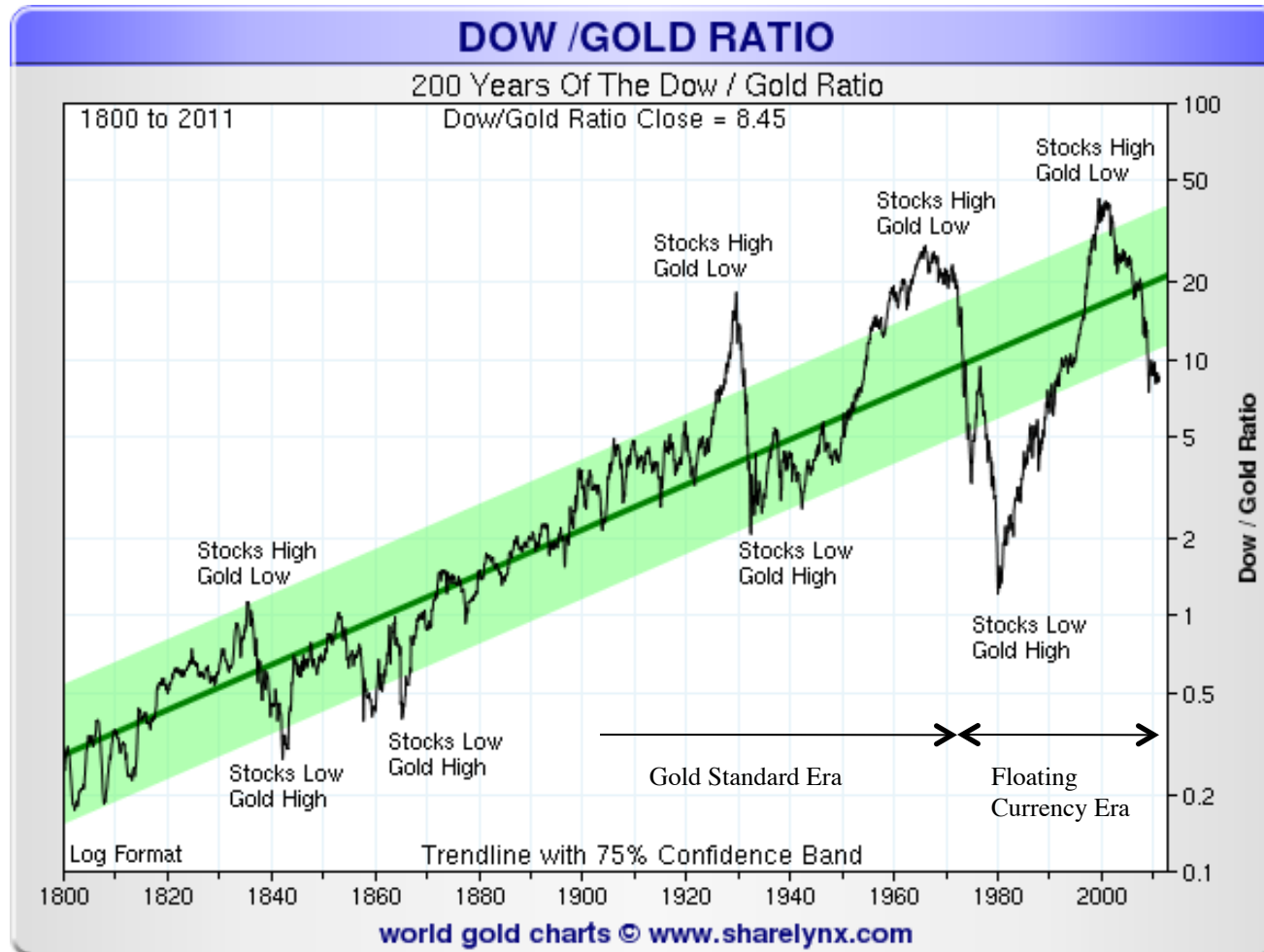
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Nothing we haven't seen before.

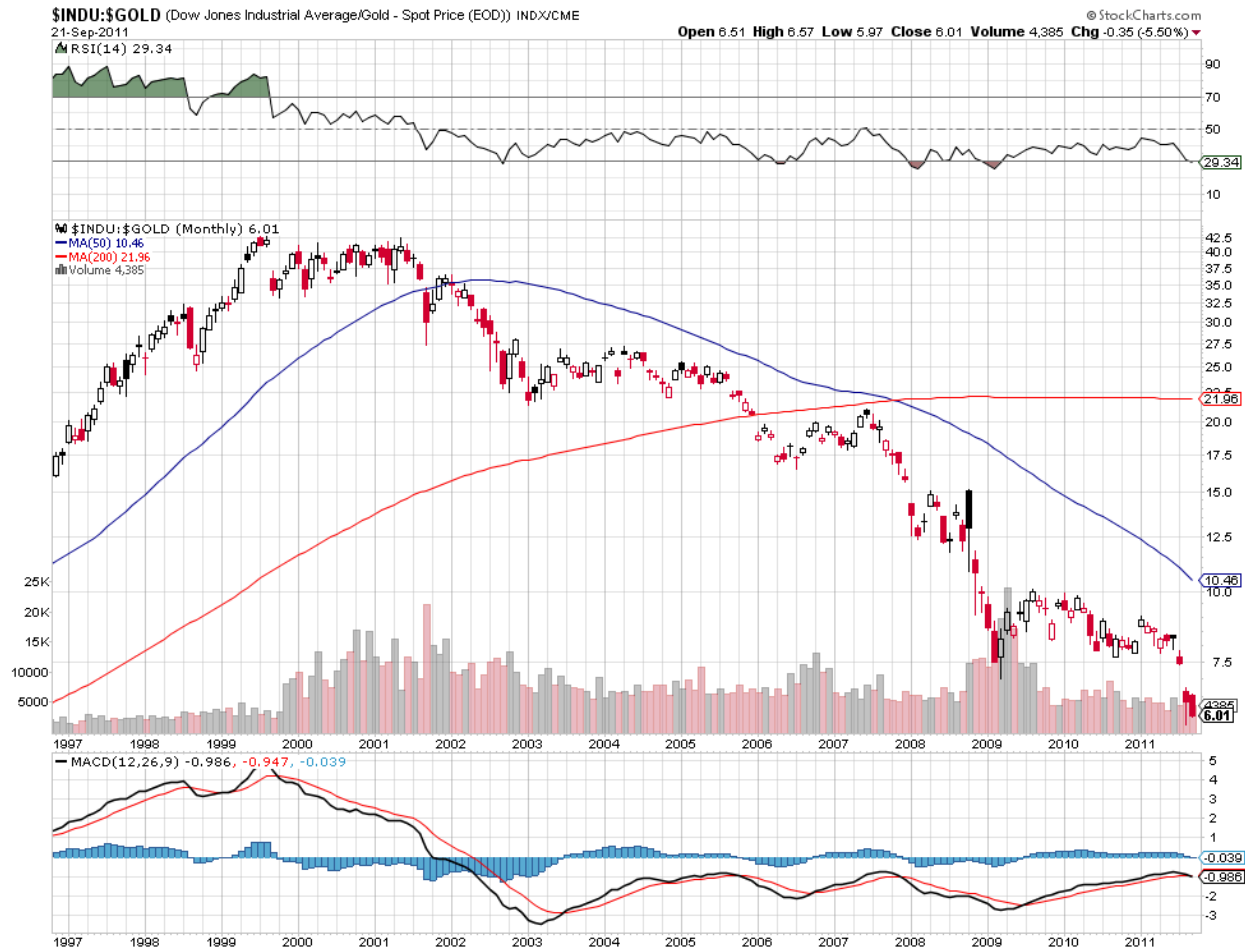




The DJIA is worth about 6 oz. of gold today = 6 \$20 1922 gold pieces = \$120 1922 dollars.



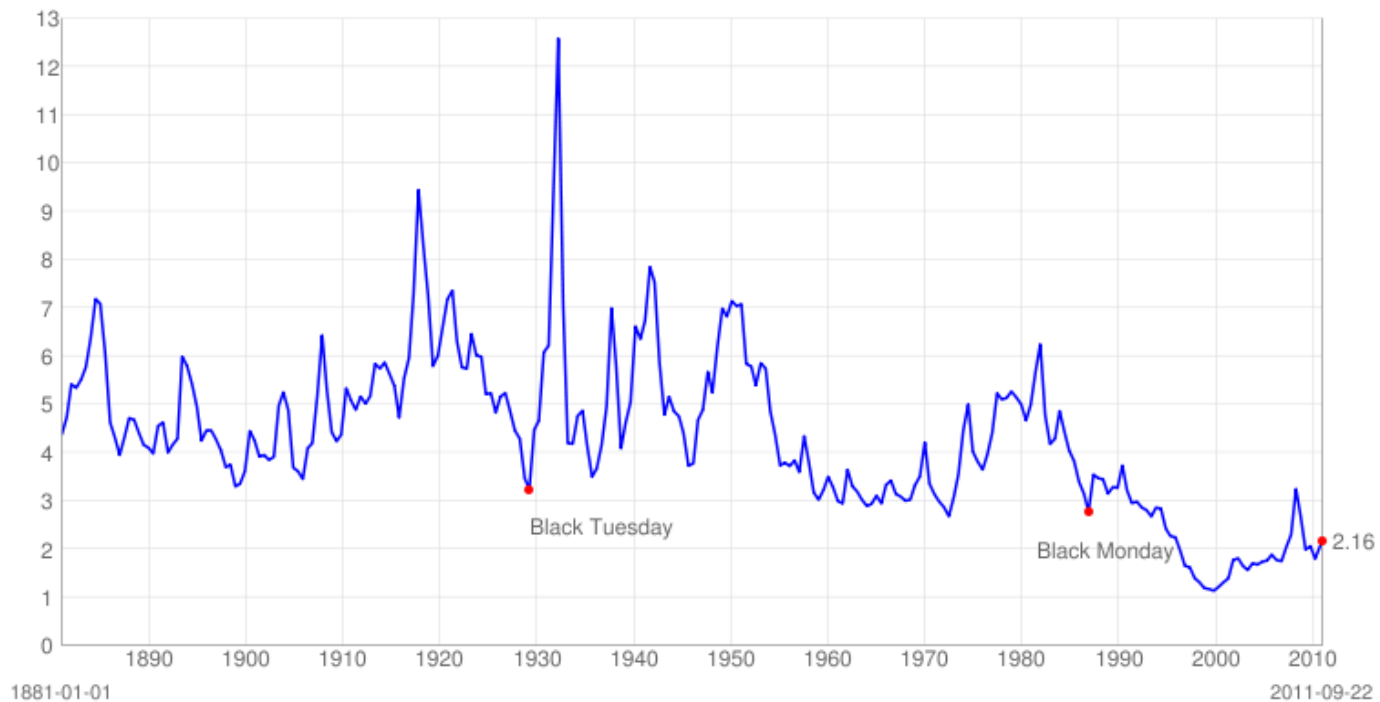
We've already had a 7:1 decline in the real value of U.S. equities.



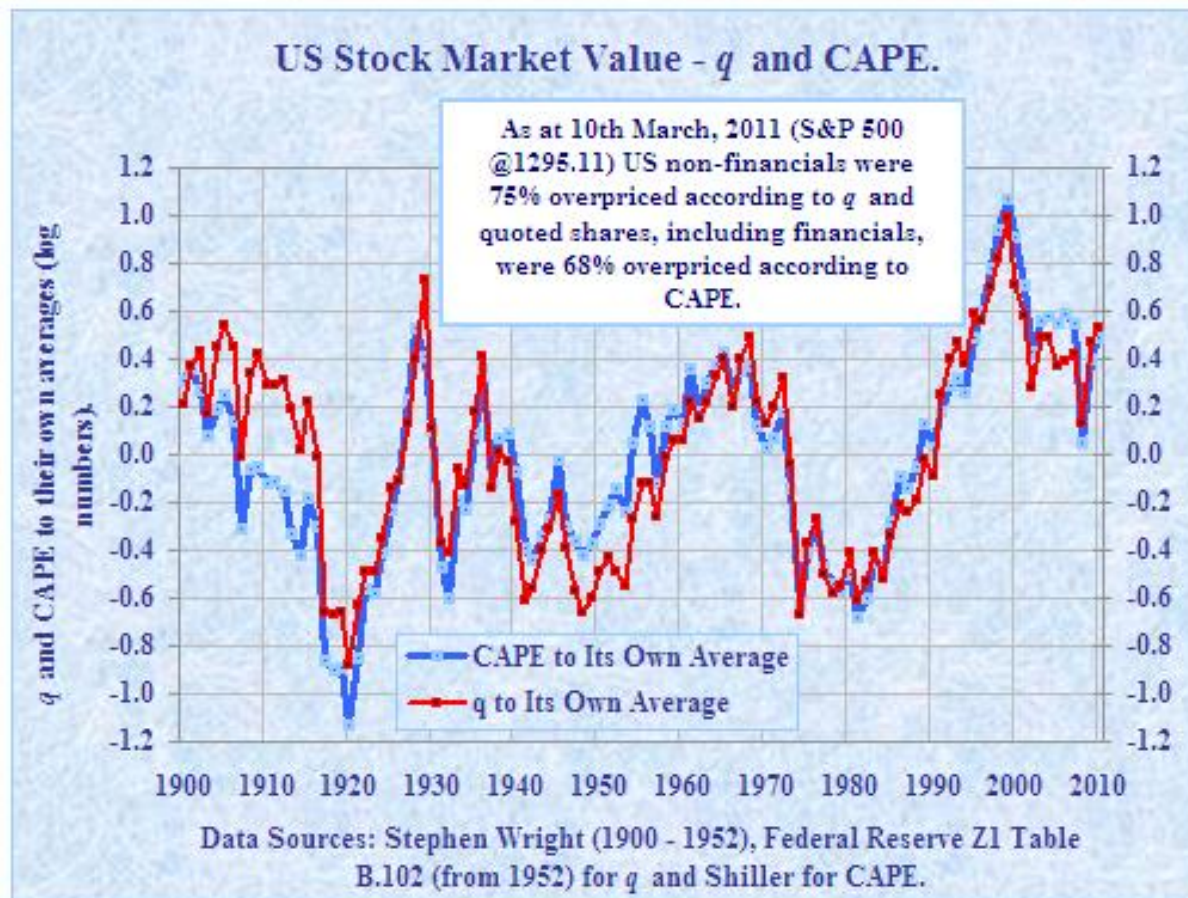
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But valuations are still frightfully high ...

The dividend yield on the S&P500 is still at a level that was never once witnessed before the late 1990s stock bubble.

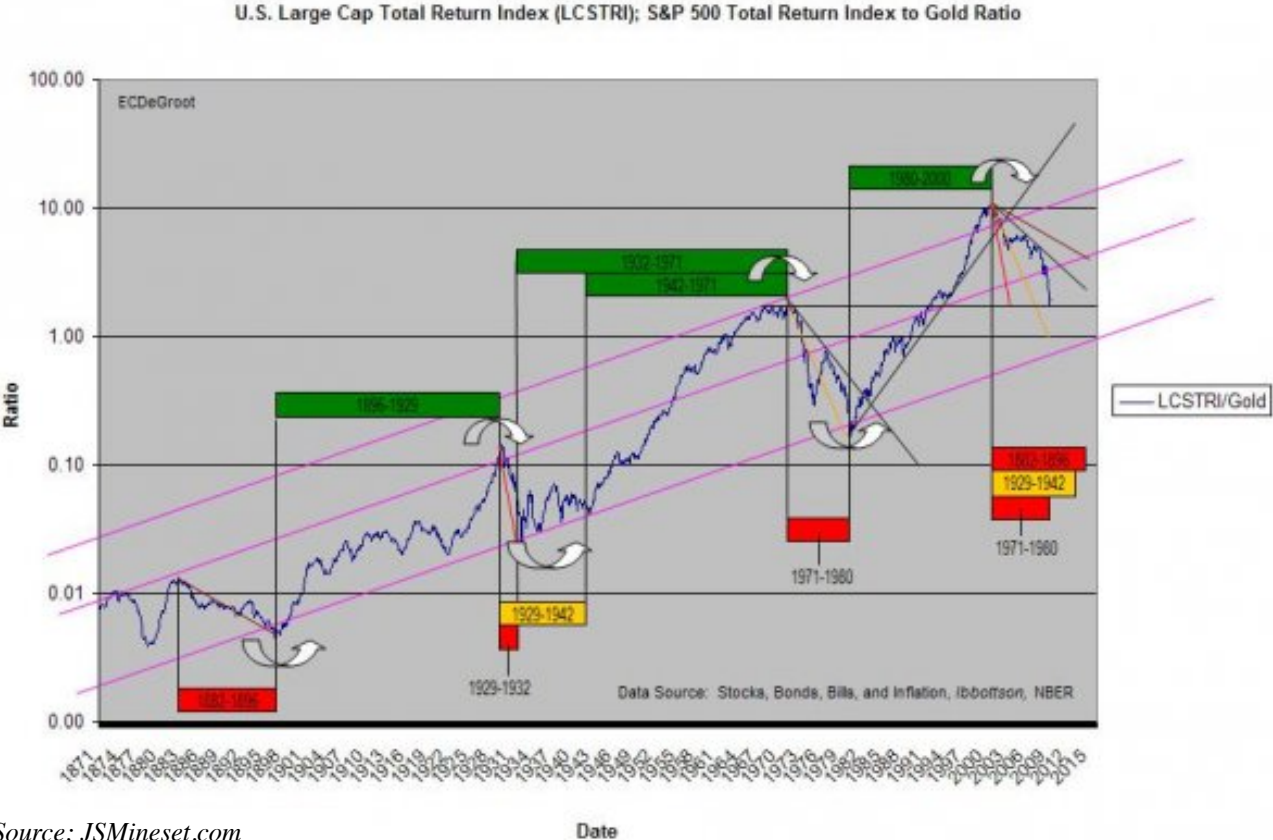


By Tobin's Q and CAPE, the most reliable long-term measures, valuations today are among the highest in history.



Source: Smithers & Co.

Since 1971 -- the era of floating currencies -- the “gold bugs” are now ahead of the “stock bugs.”

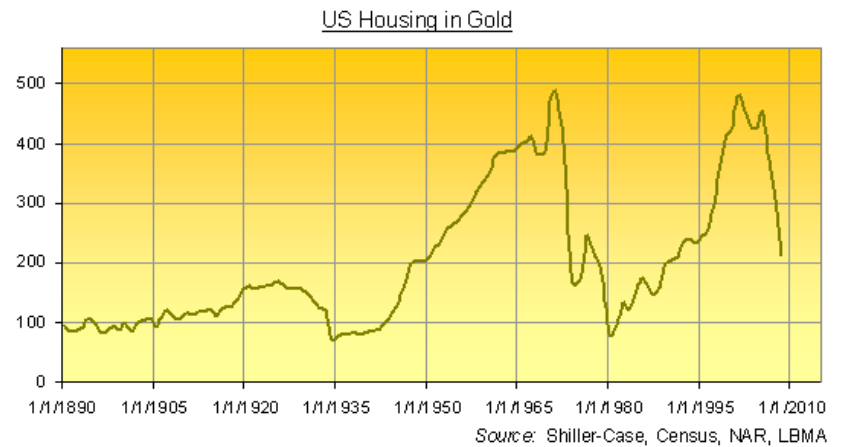
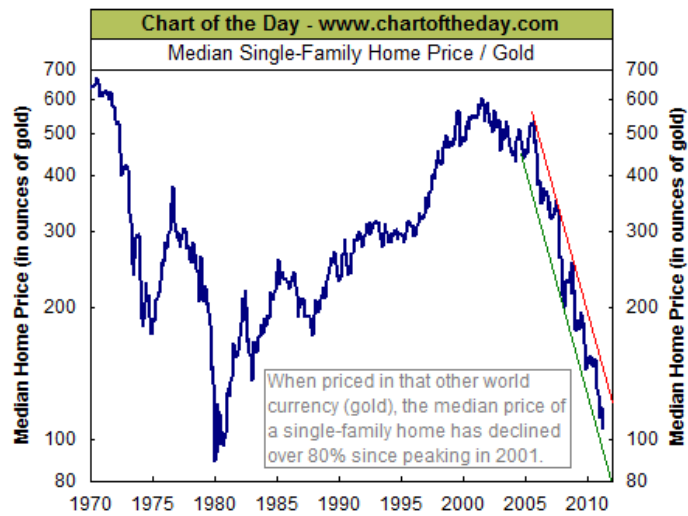


“Gold bugs” are beating “bond bugs.”



Source: JSMineset.com

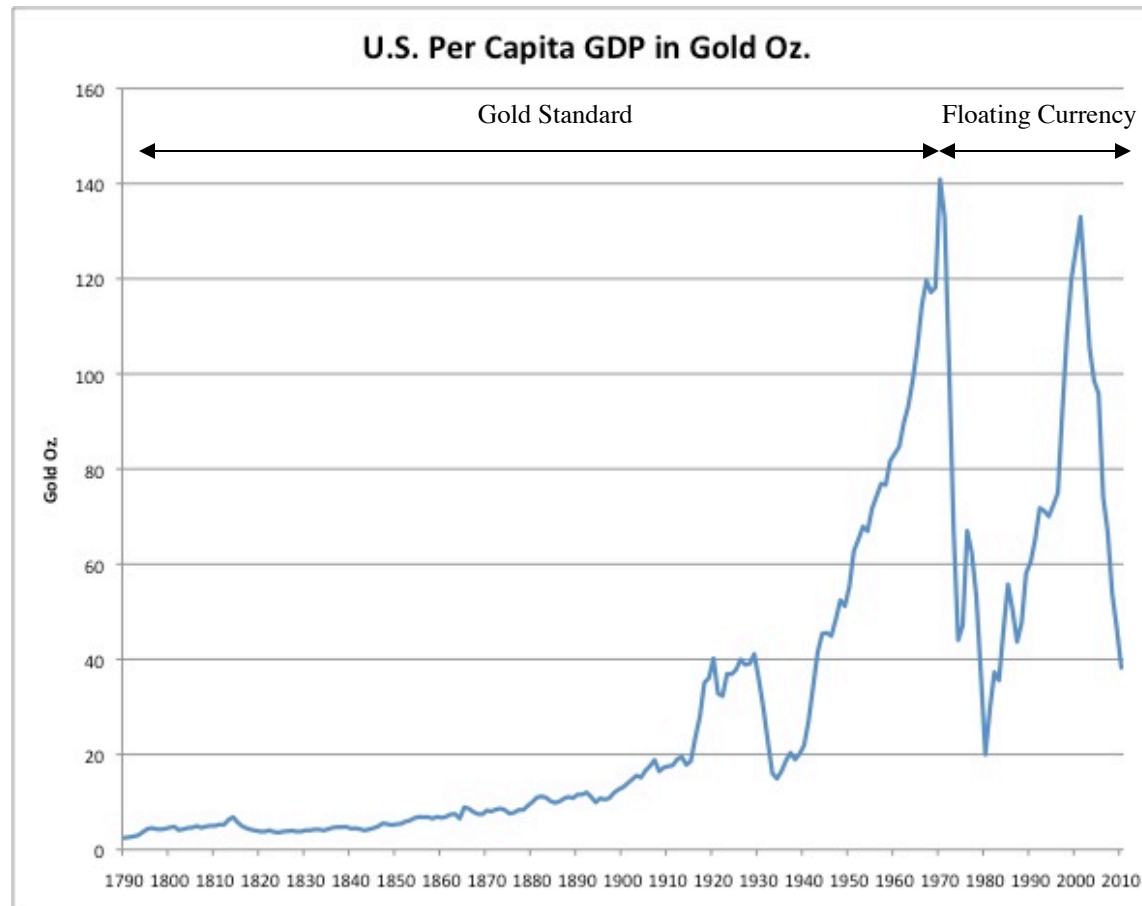
# Who says houses always go up?



Source: Bullionvault.com

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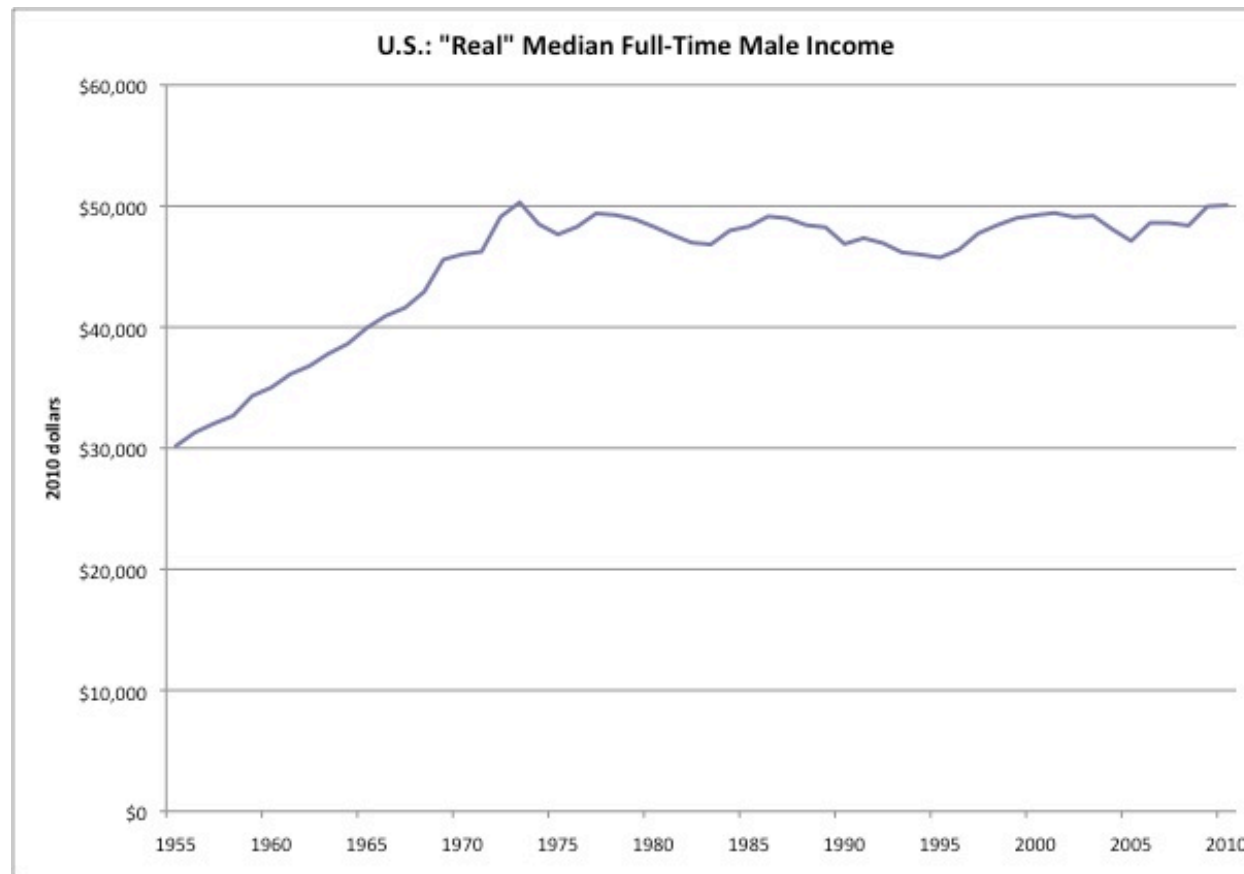
Why can't U.S. families get by anymore -- even on two incomes?





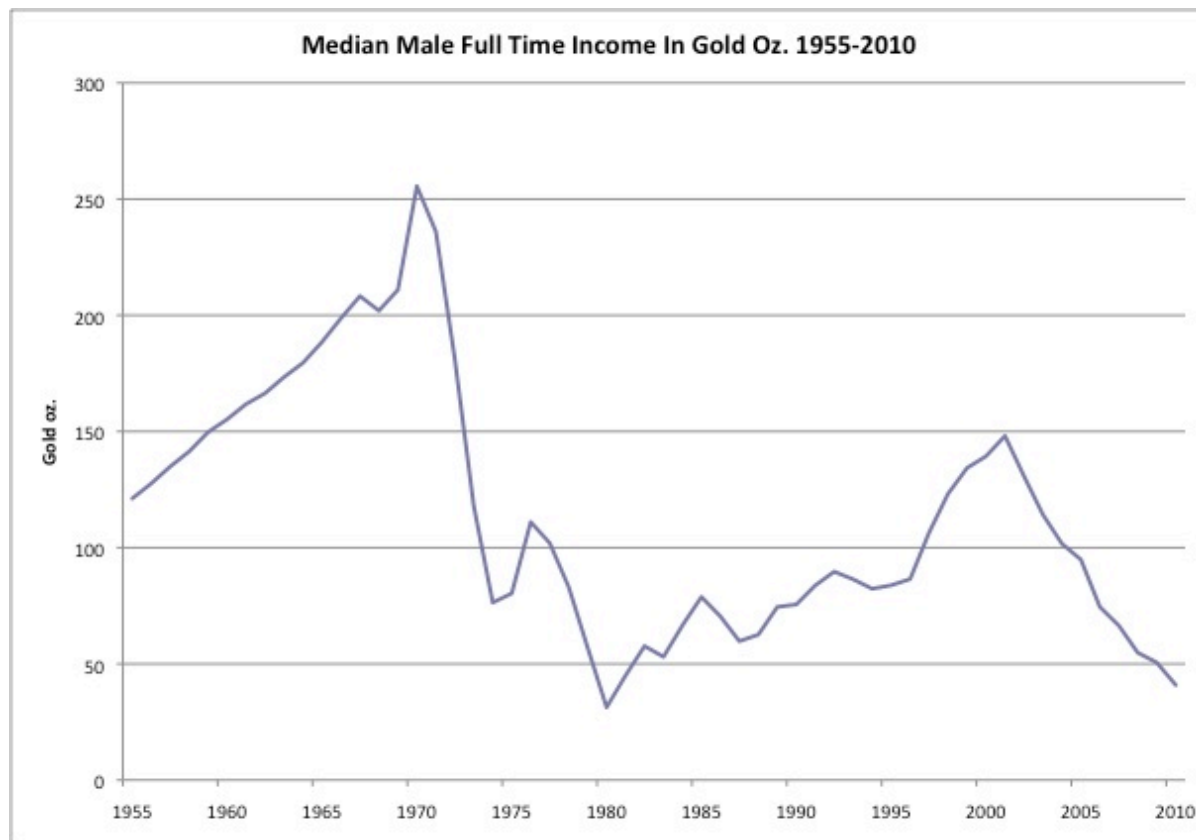
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“Real” (???) wages have been stagnant since ... the end of the gold standard in 1971.



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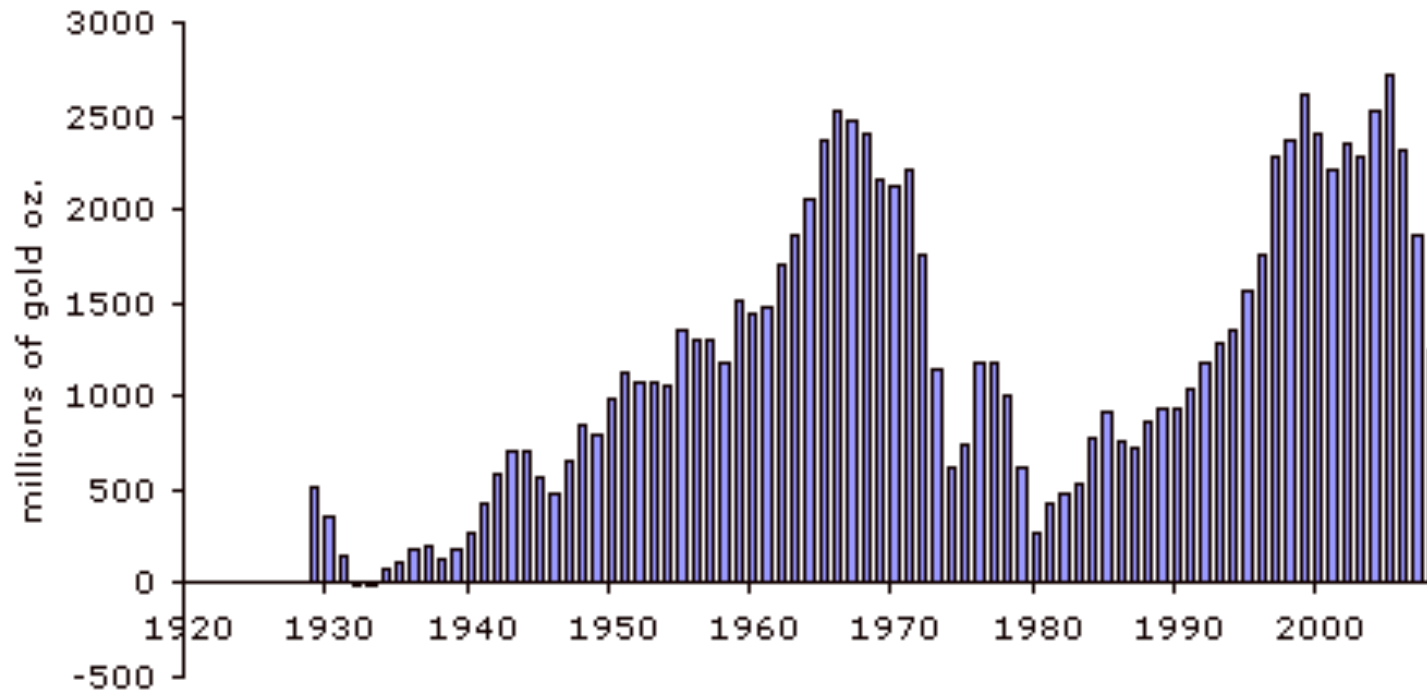
When you measure in “1922 dollars,” it looks a lot worse.



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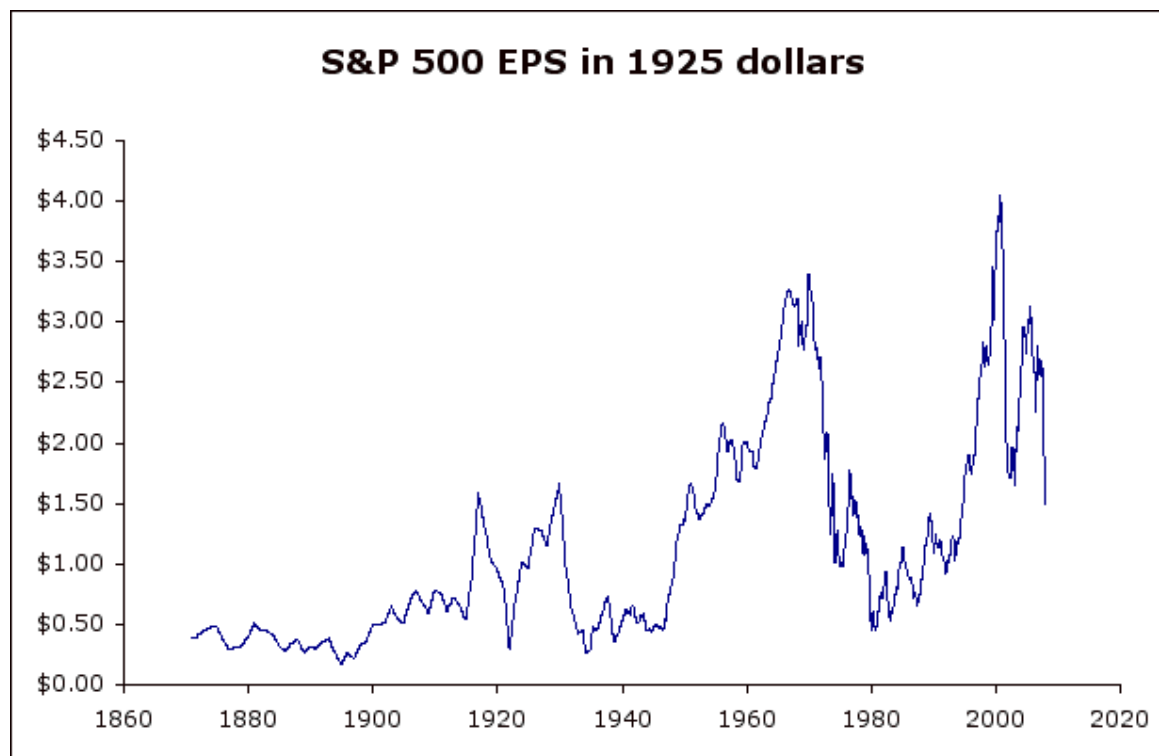
This is why the DJIA is back to 1920s levels vs. gold

U.S. corporate profits in gold oz. 1929-2008



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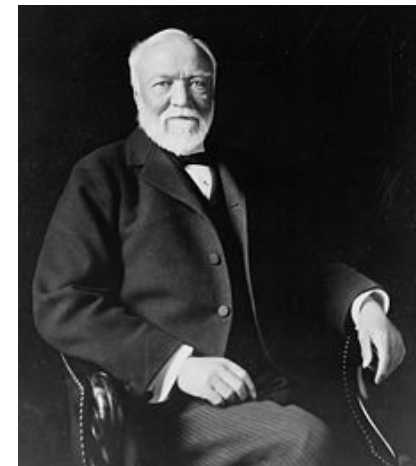
\$93 EPS (2011e) is \$1.28 in 1925 dollars (at \$1500/oz.).



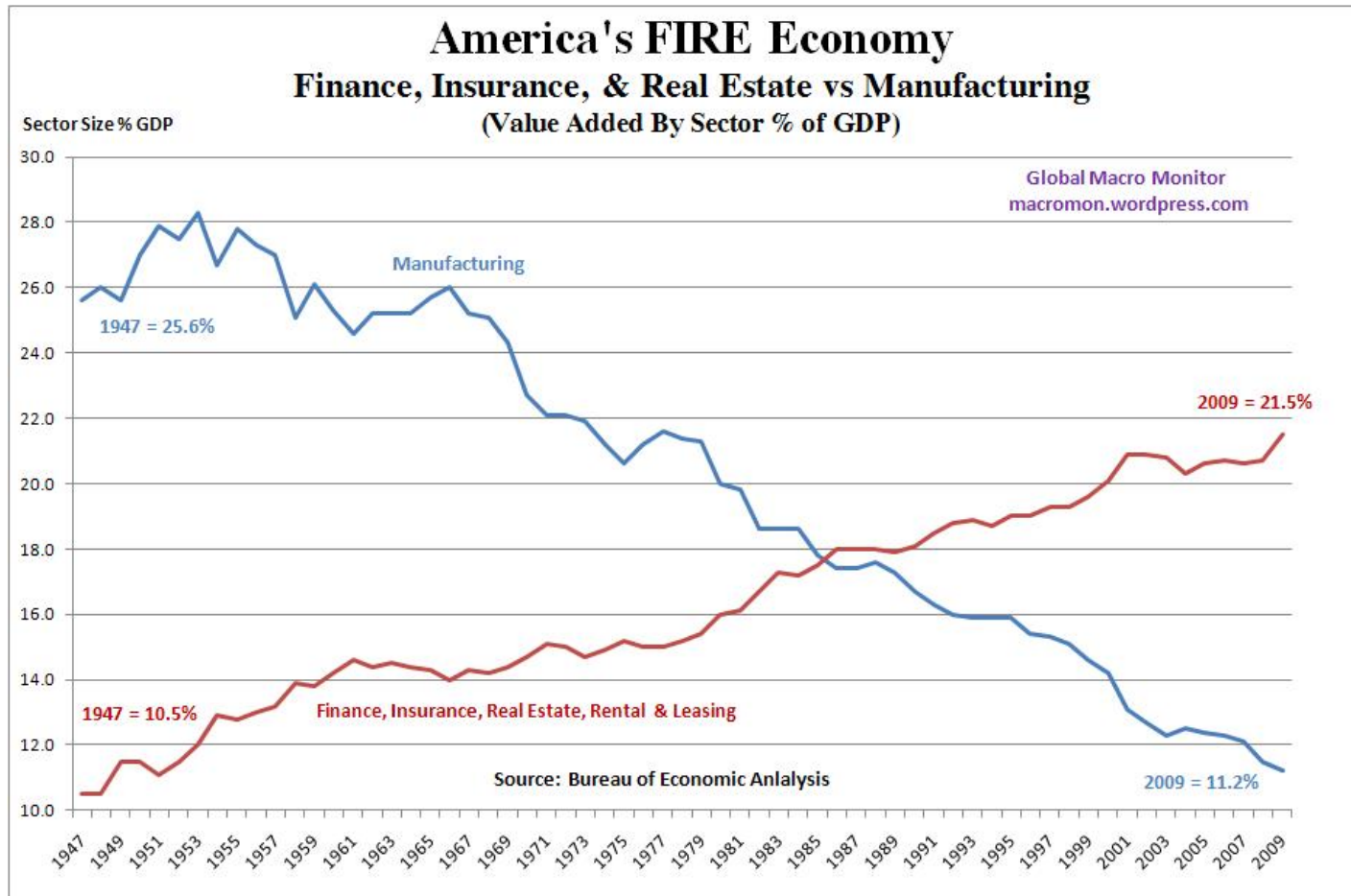
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Nothing places the farmer, the wage-earner, and all those not closely connected with financial affairs at so great a disadvantage in disposing of their labor or products as changeable "money." ... You all know that fish will not rise to the fly in calm weather. It is when the wind blows and the surface is ruffled that the poor victim mistakes the lure for a genuine fly. So it is with the business affairs of the world. In stormy times, when prices are going up and down, when the value of the article used as money is dancing about--up to-day and down to-morrow--and the waters are troubled, the clever speculator catches the fish and fills his basket with the victims. Hence the farmer and the mechanic, and all people having crops to sell or receiving salaries or wages, are those most deeply interested in securing and maintaining fixity of value in the article they have to take as "money."

Andrew Carnegie, "The A B C of Money," 1891



Does that sound like our world today?



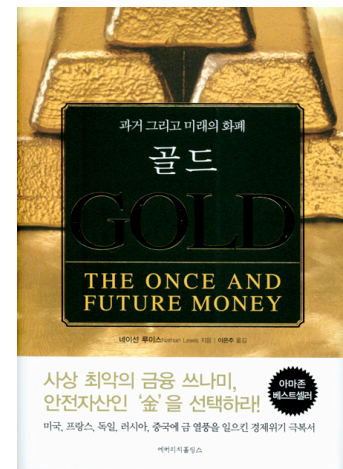
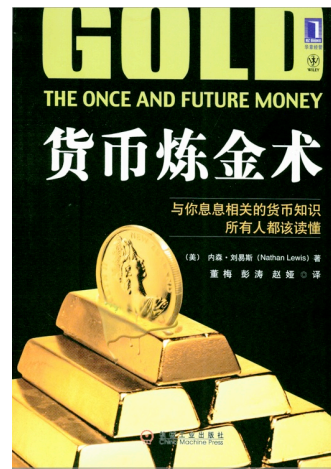
# Thank You

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Author, *Gold: the Once and Future Money* (2007)

Newworldeconomics.com



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“The one essential quality that is needed in the article which we use as a basis for exchanging all other articles is fixity of value. The race has instinctively always sought for the one article in the world which most resembles the North Star among the other stars in the heavens, and used it as ‘money’ -- the article that changes least in value as the North Star is the star which changes its position least in the heavens, and what the North Star is among stars the article people elect as ‘money’ is among articles.”

Andrew Carnegie, “The A B C of Money,” 1891

