

As Good as Gold

In one bold step, the President has the power to increase economic security, lower interest rates, balance the budget without Draconian spending cuts, and increase the stature of the dollar, both at home and abroad.

Our President can do as former President Harry S Truman did in 1944, and reinstate dollar-gold convertibility. In 1947, the benefits of a monetary standard based on gold were extended to the rest of the world through the Bretton Woods Agreement. As a result, between 1945 and 1952:

- * Private output (real GNP less defense) expanded at an average annual rate of 5.2 percent;
- * The Federal budget was in surplus for 5 out of the 7 years;
- * Treasury bill rates ranged between 0.4 percent and 1.8 percent; and
- * The rate of inflation fell from its post-World War II peak of 20 percent, to zero

The national unemployment rate never rose above 6 percent.

Since August 1971, when former President Richard M. Nixon severed the final link between the dollar and gold, economists, politicians, and bankers have run a noble experiment: a world of floating exchange rates and domestic monetary systems ruled entirely by the unchecked judgment of a few men. In return for underwriting this experiment, the American people were promised increased economic security and higher rates of economic growth. Freed from the constraints of an international gold standard, the American people were assured that the members of the Federal Open Market Committee would use their good judgment to adjust the money supply to ensure high employment, sustained economic growth, and avoid costly recessions. On the international front, Americans were promised that a floating dollar would reduce the trade deficit and ensure the international competitiveness of our workers and businesses.

With the benefit of 24-plus years of experience, it is clear that this experiment has failed. Increased flexibility and free use of judgment in the 1970s delivered a decade of the worst economic performance the U.S. has seen since the Great Depression. By the end of the decade, the U.S. was suffering from its second oil shock, an international run on the dollar, and the highest interest rates in our history. By the 1980s inflation was brought back to below 3 percent, and interest rates were reduced to below 10 percent, but the U.S. also ran the largest trade deficit in its history and the largest debt of any country -- ever.

No relief appears to be in sight for the 1990s. The Fed has raised interest rates to prevent too much economic growth and too much employment.

Political Failure

The fact that this experiment has not been brought to an end is a monumental failure in political leadership. This failure could be excused by pointing out that overall, monetary policy improved during the 1980s. In fact, by the end of 1993, interest rates were at their lowest in more than 20 years. But if we excuse this failure of leadership, we overlook the simple fact that the debate over monetary policy is at its core, *a debate over political power*. This debate has gone nowhere because it has been waged in economic terms, among politicians and a political establishment that neither

fully understands the full impact of current policy, nor welcomes a change in policy. Indeed, the movement toward establishing a gold standard will continue to go nowhere as long as the debate is being waged on the wrong front with the wrong forces.

In the 1980s, the debate over tax policy resulted in beneficial change to Americans because supply-side economists took the debate to the American people and rearticulated -- in plain terms -- how tax rates affected Americans in our daily lives. As a result, tax rate reductions gained popular support because Americans finally understood how lower tax rates would increase employment, investments, and overall opportunity. The phrase, "If you tax something, you will get less of it, and if you subsidize something, you'll get more of it. . . . today, we are taxing work, investment, and savings, and subsidizing nonwork and leisure," did more to effectively mobilize the effort to reduce tax rates than any sophisticated economic argument had before. The result was the longest period of peacetime expansion the U.S. had experienced up to that time.

The same strategy must be adopted for engaging the debate over monetary policy, and bringing about a change in current policy. Indeed, a change in monetary policy will require no less than a *popular uprising* in which the American people fully comprehend their stake in the outcome of the debate -- not unlike the tax revolt that popularized Ronald Reagan's candidacy and placed him in office in 1981. We must clearly and effectively demonstrate to the American people how the restoration of a gold standard will improve their everyday lives.

Money & Trust

Traditional economists misunderstand the true nature of money, and view it as a "thing" or a "commodity" which can be counted and measured in and of itself (e.g., " the money supply", the "monetary base", the M's). Instead, money is a human invention designed to facilitate trade and commerce, and based in trust. Money is also a tremendous tool of coordination. Our modern market economy and the transactions that occur within it would not be possible without the invention of money. Money provides a universal substitute for the human exchange of providing a good or a service for another good or service.

Traditional economists fail to understand that the phenomenon of money is one that is intrinsically based on trust. People accept money in exchange for goods and services because they trust that someone else will in turn, accept the money in exchange for an equivalent amount of goods and services. Likewise, when people lend money to others, they do so trusting that they will be repaid in money that will be exchangeable into goods and services. Money is useful only because we trust the promise of exchangeability. Trust is built when a promisor recurrently keeps his promises.

Money then can be seen as a kind of promise between the government and the people. When the promisor is trustworthy, people believe in the promise, they hold the money. Interest rates are low, prices are stable, and the currency is considered strong. On the other hand, a currency devaluation, such as the recent Mexican devaluation, is a betrayal of the government's promise to maintain the value of money. This promise, once betrayed, destroys trust - which is very hard to rebuild.

Why gold?

Why use a monetary standard based on gold? Because gold has a history of having remarkably stable purchasing power in terms of all other goods and services. Gold acts as a substitute for the price of goods. For example, an increase in the price of gold indicates an increase in the future rate of inflation. Most importantly, gold enables all of us to observe whether or not the government is fulfilling its promise to maintain the value of our money. The fulfillment of this promise over time builds trust, leading to lower interest rates, stable prices, and strong currency.

One can only imagine the benefits which could be realized and opportunities created from the implementation of an international monetary system in which currencies are stable and interest rates low:

- * Families and individuals could once again purchase homes at mortgage rates under 6 percent;
- * Business growth could once again increase through start-ups and expansion with the prime rate at 4 percent;
- * Corporations could once again create new jobs and lower unemployment by borrowing at long-term rates as low as 5 percent;
- * Resources now committed to hedging foreign currency exposure and interest rate volatility could be freed to provide tangible benefit to Americans;
- * Billions of dollars of losses in bond derivatives could be avoided by the elimination of the need for such esoteric financial instruments. and

Our futures would once again be secure with the knowledge that returns on investments made today will be repaid in dollars that buy as much in 30 years as they do today.

These benefits are surely as possible today, as they were when President Truman reinstated dollar-gold convertibility during those uncertain times following World War II. All that is required by our President, whoever he may be, is the wisdom to learn from the past, and the courage and leadership to act on behalf of the future.