

SILVER & GOLD REPORT

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The Nobel Prize-winning economist who forecast the 1929 Crash tells our readers now —

“I see very little similarity between 1929 and today. I don't expect another crash. Instead I see repressed inflation, which can be worse.”

— F.A. Hayek

In this exclusive SGR interview, Dr. Hayek explains why he believes we're not headed for a 1929-type crash — but why instead he forecasts continued inflation, economic stagnation, and a very long, painful recession. Surprisingly — for one of the great hard money economists — Dr. Hayek opposes a return to the gold standard. His alternative is a radical new proposal for denationalizing money. In conclusion, Dr. Hayek offers specific advice on personal investments in currencies and gold. He cautions, “Don't be patriotic in monetary matters. Choose the money which helps you best.”

Dr. Hayek was born in Vienna on May 8, 1899. He served as an officer in World War I and afterward studied at the University of Vienna where he became a Doctor of Law in 1921 and a Doctor of Political and Social Science in 1925. After two years in the civil service of Austria, he became the first director of the Austrian Institute of Economic Research in 1927.

In 1931, he was appointed to a chair in economics at the University of London and was later awarded a Doctorate of Science in Economics there. From 1950 to 1962 he held a professorship at the University of Chicago. Then from 1962 to 1968 he was Professor of Economic Policy at Albert-Ludwigs University in Freiburg, West Germany.

Dr. Hayek's most important books include Prices and Production (1931), Monetary Theory and the Trade Cycle (1933), Collectivist Economic Planning (1935), The Pure Theory of Capital (1941), Individualism and Economic Order (1948), The Counter-Revolution of Science (1952), and The Constitution of Liberty (1960).



Dr. F. A. Hayek

His best-known book is *The Road to Serfdom*, whose main thesis is that centralized governmental planning is not only less effective than a free market economy, but also leads inevitably to totalitarianism. First published in London in 1944, *The Road to Serfdom* became a best seller in both England and America, was translated into 12 languages and condensed by the Reader's Digest.

Even John Maynard Keynes, the leading pro-centralization economist of the day, gave *The Road to Serfdom* an almost passionate endorsement, writing that he was "in deeply moved agreement" with Dr. Hayek's point of view.

During recent years, Dr. Hayek has been writing a three-volume work, *Law, Legislation and Liberty*. He's also developed the idea of a private-enterprise system for international currency. This concept is expressed most completely in his *Denationalization of Money*, published in 1978 by the *Institute of Economic Affairs*, London.

Our first interview with Dr. Hayek appeared in June 1975. SGR recently taped a second interview with Dr. Hayek at his home in Freiburg, West Germany.

"A very unstable condition was created in 1927 when the Federal Reserve tried to stave off a collapse by credit expansion."

SGR: Dr. Hayek, you were one of the very few economists of the 1920's who predicted the Great Depression. How were you able to forecast what would happen in 1929?

HAYEK: I did say in print, in February, 1929 that there was no hope for economic recovery in Europe before American interest rates came down. That wouldn't be until the American boom collapsed — which was likely to happen within the next few months. And this did, in fact, happen in October 1929.

What made me expect this, of course, was one of my main theoretical beliefs — that an inflationary boom cannot be maintained indefinitely. I was sure that a very unstable situation was created by the artificial prolongation of the boom in 1927, when the Federal Reserve tried to stave off a collapse by credit expansion.

America was still on the gold standard then, so of course there were limits to inflation — because the money supply couldn't be expanded indefinitely. Under the gold standard, an inflationary boom couldn't last very long — sooner or later

it would have to stop and then the whole thing would crash down.

SGR: Do you see any similarity between the 1920's and the situation today?

HAYEK: Very little. I don't believe we're in for a crash now. It's much more likely that government will just conceal the continuation of inflation by price controls. But if anything is worse than an open inflation, it's a repressed inflation. What you're likely to get is not a violent deflation but increasing stagnation of productivity.

SGR: Why doesn't the US government stop inflation?

HAYEK: You must stop inflation rapidly and suddenly. It's painful, but it can be done.

For example, very few people remember now that in 1921, when prices were 50% above pre-

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war level, the Federal Reserve got them down below the pre-war level in six months. This was a very painful period but it didn't last long. By the end of the year another boom was in the making.

True, it's technically possible to slow down inflation gradually — but it's politically impossible. No country will stand a dragged-out misery.

Yet politicians always choose the politically less dangerous process of trying to cure inflation gradually. They fail every time and it causes much more pain in the long run.

“If the world as a whole returned to the gold standard there would be such fluctuations in the value of gold that it would very soon prove impractical.”

SGR: As you said earlier, Dr. Hayek, the gold standard places limits on inflation. Do you foresee any chance of return to the gold standard?

HAYEK: No. And I wouldn't advocate it.

No single country can restore the old gold standard. It was essentially based on different countries making their currencies convertible into a certain weight of gold.

I'm afraid there is just not enough gold about to bear the strain if the majority of countries tried to return to a gold standard.

At first there would be a rush for gold. But if the world as a whole returned to the gold standard there would be such fluctuations in the value of gold that it would very soon prove impractical.

Today an international gold standard could only mean that a few countries would maintain a real gold standard. The other countries would hang on to the system through a gold exchange standard — where the currency isn't really redeemable in gold but the government attempts to keep a fixed rate between its currency and gold.

“The gold standard gave the world one long period of relative stability — 200 years or more — during which modern industrialism could develop.”

I just wouldn't trust any government to maintain a stable currency. Government historically has kept currency stable only under compulsion. When the gold standard was in ascendancy, it was an important matter of national prestige to maintain it and to be driven off gold was a national disgrace. This gave the world one long period of

Dr. Hayek on OPEC and inflation

“OPEC is no excuse for inflation at all. Oil prices cannot cause inflation unless you give the people more money. If you attempt to deceive the people by giving them enough money to buy all the gasoline and everything else they ever wanted, then naturally the effect is inflation. If the money supply wasn't tampered with, what should happen in the market is that when oil goes up, other prices must come down.”

relative stability — 200 years or more — during which modern industrialism could develop.

But as soon as it became widely understood some 50 years ago that convertibility into gold was merely a method of controlling the *amount* of a currency — which was the real factor determining its value — governments became only too anxious to escape that discipline. And money became more than ever before the plaything of politics.

“If a big country like the United States did return to the gold standard, it would start a great deflation.”

SGR: As you know, Ronald Reagan has come out in favor of some form of return to the gold standard for the U.S. Suppose we imagine that Reagan is elected President and he calls on you for advice. What would you tell him?

HAYEK: Again, I would advise against the gold standard. If a big country like the United States did return to the gold standard, the effect on gold's value would be so serious that it would start a great deflation. Most likely the government couldn't stick to it for long. They'd switch the policy to some halfway measure like a gold exchange standard.

SGR: Then what would you recommend?

HAYEK: I would recommend to begin by instructing the Federal Reserve to control the quantity of money so as to keep the price of gold approximately constant. Then gradually substitute for the price of gold an ever-widening index of different commodities.

And to this I'd add that everybody else is allowed to compete with the Federal Reserve by issuing another index money.

SGR: But has private issuance of money worked in the past? What about American “wildcat banks” of

the 1830's? They circulated worthless banknotes far and wide.

HAYEK: All those wildcat banks were issuing dollars. That wouldn't do. The public must be able to clearly distinguish between the different kinds of money. I don't advocate allowing people to compete in issuing currencies with the same name.

If you had private issues of currencies, each with its own distinct name, there would be clear currency exchange rates where you could see at once if any one depreciated. Then people would either try as hard as possible to get rid of that money, or the issuer would try very hard to correct the problem.

This process of selection would insure that only stable money remained in the market and all unstable currency would be happily eliminated.

But the kind of system that existed in many parts of the world at different times where different agencies were in competition issuing money of the same name — can't possibly work.

“You can't manufacture Kodak products unless you're Kodak. Individual brands of money would have this same protection under existing trademark laws.”

SGR: How would you prevent private issuers from doing exactly that, in a free society?

HAYEK: Just give the issuer a trademark to protect his individual brand of money. This can be done under existing law.

SGR: And it would be a violation of the fraud laws to imitate the original private issuer's brand of money?

HAYEK: Of course. Take just the trademark law. You can't manufacture Kodak products unless you're Kodak.

... My whole plan, you see, is a sort of stand-by proposal if our system collapses completely. I hope I won't live to see this, but it may not be far away. I think this is a very critical period for the West.

I have a phrase which I will repeat here: If the politicians don't destroy the world in the next 15 years, I'll be very hopeful.

I'm by no means certain we won't have a major catastrophe in the next 15 years. But if we don't, I'd be very hopeful because I find among the young a marked reaction against all socialist tendencies. When the generation which is still only in its 30's comes to power, I think we can hope that

they will be more sensible than the present statesmen.

“Even if the government puts the death penalty on the possession of gold, as the Nazis did, it won't prevent people from burying gold in their garden.”

SGR: Turning now to personal investing, if we may: What advice would you have for our readers?

HAYEK: The advice I would give is: If you have the courage to do so, don't feel patriotic in monetary matters. Choose the money which helps you best.

When I look at the world, I sometimes feel that here in Germany one may still be in some sort of lifeboat that can hope to keep afloat when the rest of the world goes bust. German and Switzerland and perhaps Austria and Belgium have the few relatively stable currencies in the world.

I don't think there is any danger of a major depreciation of the German mark. The German people are very sensitive about inflation. A whole generation lived through the Great Inflation here, after all. Any real scare of a return to inflationary conditions would cause a much more violent reaction in Germany than in any other country. I think if tomorrow the papers told the Germans the mark had depreciated about 10%, the government would be out overnight.

However, unless the monetary system is very thoroughly changed, government inflation in most countries will go on at an accelerating rate. There will be periods of price control that won't succeed in solving the problem. The general tendency will be for dollar prices to go up, and for gold prices to go up.

But don't *speculate* in currencies and gold. There will be violent fluctuations of value. All I can promise is that the people who speculate are going to burn their fingers.

In closing, let me just go back to something I told your readers a few years ago in our first interview:

Even if the government puts the death penalty on the possession of gold, as the Nazis did, it won't prevent people from burying it in their garden to have something of value when the government has changed. To have something that will still be of value in 20 years time is, for the great majority of people, still very important. ■

Mexico report

Promised repeal of Mexican 40% mining profits tax bogs down in "usual bureaucratic delays"

by Emil Zubryn
SGR Mexican Correspondent

The Mexican government's promised repeal of a new 40% tax on silver and gold mining profits [reported in the Late September 1980 *SGR*] has gotten bogged down in the usual bureaucratic delays. It remains to be seen how soon the promised tax relief will go into effect — and how far it will extend.

The 40% tax has been denounced as a damper on new production increases by the World Silver Institute, the Mexican Mining Chamber, regional mining organizations, and many individual gold and silver mines of all sizes.

Mining of low-grade silver ore is at a standstill.

The President of the World Silver Institute, Bernard Rohe, recently told a meeting of the Mexican Association of Mining Engineers, Geologists and Metallurgists that the tax is holding up development of Mexico's vast reserves of low-grade silver ore deposits.

Rohe said that continued major investment by Mexican silver miners is necessary in order to extract the silver available in low-grade ores. This investment in costly equipment and facilities is being put off by mine owners due to the 40% profits tax.

Some 80% of Mexican silver production is a byproduct of copper, lead and zinc mining. Without the 1980 tax on profits, a silver price of \$20 per ounce would be sufficient to open up development of the country's many large low-grade deposits, Rohe said.

During the past three years, Mexican mining interests have invested just over \$2 billion to expand production. Another \$2.2 billion scheduled to be invested during the next two years will probably be withheld as long as the tax lasts, said Ricardo Rojo, commercial director of Penoles de Mexico mining complex. ■

House Notes

***SGR welcomes Dr. Franz Pick as our newest contributing editor.** Dr. Pick is one of the greats of the hard money movement. Bankers, politicians, authors, and corporate executives regularly seek him out for advice.

Mocatta Metals President Henry Jarecki and best-selling author Harry Browne, for example, are two of the many hard money leaders who publicly acknowledge their debt to Dr. Pick's pioneering insights.

Dr. Pick — 82 years old and feisty as ever — is no stranger to our pages. We've interviewed him every year since 1976 and our readers have found these interviews extremely valuable. But now you'll be able to read Dr. Pick's latest insights and advice about silver and gold in *SGR* every month.

Dr. Pick studied law at the University of Leipzig, currency theory at the University of Hamburg and inflation theories at the Sorbonne in Paris. His degrees include BS, MA, MBA, LLD, and PhD.

Dr. Pick is the publisher of *Pick's Currency Yearbook*, a standard reference work that comprehensively reviews some 113 currencies annually. He also publishes *Pick's World Currency Report*, a monthly publication noted for its authoritative assessments of global currencies.

***Your next SGR issue will be late.** We are delaying it so that we can bring you exclusive, in-depth coverage of the 1980 NCMR New Orleans Conference.

The NCMR (National Committee for Monetary Reform) Conference is the "big daddy" of hard money conferences — and it promises to be so again this year. It begins the day after the Presidential election. A major topic of discussion by the experts will be the election's probable effect on silver and gold prices.

The five-day conference ends on November 9. **Your next issue of SGR will be dated Mid November 1980. It will be mailed to you during the third week of the month.**

IMF Conference 1980:

Annual conclave of begging bowls speeds destruction of paper currencies — de facto guarantees higher gold prices.

by Dr. Franz Pick
SGR Contributing Editor

Some 4000 people, most of them monetary illiterates and virtuosos of political corruption, converged on Washington D.C. early in October to take part in the annual conclave of begging bowls — officially known as the 1980 meeting of the International Monetary Fund and World Bank.

Decisions emanating from the IMF this year were a silly attempt to sanctify printed paper as the ultimate value — in hopes of permanently replacing stable currencies with an artificial credit system.

Yet in fact the IMF succeeded in doing exactly the opposite of what it intended. Not only did it virtually lock in worldwide inflation — the IMF also drove the last nail into the coffin of debased paper currencies.

The dominant force which has taken over the IMF is the pressure exerted by the underdeveloped countries. They simply demand more and more money without question — regardless of their lack of credit worthiness. Naturally, the threat implied in each stepped-up demand for alms is that otherwise they will go under financially. Then the entire world's economic structure would crash down around the industrialized powers.

The mood of the 1980 IMF was best summed up by India's Finance Minister, R. Venkataraman, who said, "We face a dangerous deflation that could turn into world depression. At this juncture a little more inflation is a lesser danger."

SDRs are a purely artificial bookkeeping unit — created out of thin air

The governing Interim Committee of the IMF is vastly experienced at giving in to the demands of the underdeveloped nations and was able to lay out an entire inflationary program before the general meeting started.

The Interim Committee's solution, obviously, was nothing more than yet another vast expansion of the international debt-creating machinery.

The IMF and World Bank will again issue and loan more Special Drawing Rights (SDRs) over and above the regular line-of-credit quotas established for each borrower country.

These quotas are a joke in themselves. In the current session, the IMF made it possible for debtor members to borrow *up to 600% of their quotas* over a three-year period. This is a boost from the mere 125% of their quotas they used to be able to borrow annually in currencies relatively stronger than their own.

As for SDRs, they are a purely artificial bookkeeping unit with absolutely no backing of real economic resources. The SDRs are created out of thin air — the exact global equivalent of the way the US Federal Reserve creates new mini-dollars out of thin air in paying for the US treasury bonds it buys.

OPEC refuses to be a pawnbroker

Heretofore, the Fund always insisted on austerity measures — deflation and devaluation — to stabilize the currency of any country requesting bail-out monies. This year, however, the IMF also acted to loosen credit terms for the borrower nations.

Now, the IMF will be no better or worse than any sleazy pawnshop that lends money on questionable collateral.

This may well have been the final straw that made some of the key OPEC countries refuse to contribute to this year's kitty. Instead, the IMF has been forced to swallow the political embarrassment of standing in line at commercial banks and the capital bond market to raise funds.

The IMF is seeking to float billions of dollars in bond issues denominated in SDRs. It remains to be seen who will be foolhardy enough to buy them — not only is the SDR a mere bookkeeping cipher, but the IMF also cannot be sued in court for default of payments.

Perhaps the only inducement that would make such debt certificates acceptable would be for the IMF to pledge as collateral some of the 103 million ounces of gold it still holds.

IMF gold sales will not be resumed

Of course, it was not so long ago that the IMF, under heavy-handed pressure from the US Treasury, was selling gold every month to smash the price of the yellow metal.

Therefore, the IMF's only positive achievement during 1980 is that the massively futile sales of gold will not be resumed. It is not lost upon even the gentlemen who run the IMF that their reserve of 103 million ounces of gold is the only thing that still summons them any respect whatsoever from the world financial community.

And despite the best efforts of all the governmental anti-gold brigades — who cling to power by lying about their mostly fraudulent paper currencies — gold and the other precious metals continue to provide the only immunity against the disease of worldwide monetary debasement.

So naturally, everything that the IMF does to help speed up the tempo of currency debasement is also a de facto guarantee that the value of gold and the other precious metals must continue to rise. Certain events quietly taking place in the market now seem to indicate that a major new upward move could be in the making.

OPEC's and Russia's unusual Swiss gold bullion transfers

Well before the sound of gunfire erupted along the Persian Gulf, Iraq had shipped home 74.6 tons of its Swiss gold holdings while Iran withdrew 17.7 tons.

Other OPEC powers may have had some small inkling that war was coming into their backyard. Kuwait shipped home 32.5 tons of the yellow metal from Swiss vaults, the United Arab Emirates withdrew 21.3 tons and Saudi Arabia took out 7.9 tons.

Aside from these movements, the OPEC powers have also bought some 250 tons of gold from South Africa and Russia so far this year.

Meanwhile, the Soviet Union shipped *into* Switzerland only a surprisingly low 5.87 tons of bullion for sale this year. Yet Bulgaria — which is

neither a gold producer nor is known to have vast gold reserves — consigned no less than 27.1 tons to the bullion dealers of Zurich and Geneva. Was Sofia acting as a middleman for Moscow?

An even more intriguing question has arisen regarding the world's No. 2 gold producer. Is Russia going to join with the No. 1 producer, South Africa, to control marketing of the yellow metal?

Pretoria's maneuvers in the bullion markets have begun to look like those of a monopoly controlling supply and demand. South Africa withheld 70,000 ounces during July and August alone.

A super-cartel in gold?

Half-confirmed reports spoke of informal contacts already made with Moscow by the De Beers combine. De Beers controls some of the biggest gold mines in South Africa as well as holding a monopoly on the world diamond market.

De Beers is as ultra-secretive as the Russians. It has operated the world's most successful monopoly for 45 years, masterfully controlling and sharply limiting any decline in diamond prices.

A new cartel arrangement between De Beers and the Russians could effectively control the amount of bullion reaching the markets. *This would radically alter existing price trends.*

Handsome profits yielded by silver-gold ratio

Handsome profits have been yielded during these past weeks to a number of operators who simultaneously sold gold short and bought silver, successfully playing the silver-gold ratio.

The silver-gold ratio was seemingly stabilized at around 39 ounces of silver to one ounce of gold. But by the end of September it had lowered to 32-to-1.

Traditionally, when the ratio is more than 37-to-1 a short position in gold and a long position in silver have generally turned out very well.

In such so-called "spread" operations, a major consideration is that the contracts didn't match up perfectly. A rise of only \$1 per ounce on a 5000-ounce silver futures contract would generate a \$5000 profit, while on a 100-ounce gold futures contract a \$50 per ounce increase was needed to produce the same profit. ■

Latest SGR market update and recommendations —

Bearish factors have seemingly spent their force . . . Downturn is near the bottom

Under pressure from the sudden outbreak of the Iraq-Iran War, gold made a sharp upturn. It zoomed past the \$700 mark for the first time since February and peaked briefly at \$722.

Then bearish factors took over and for approximately one month the predominant trend has been down. At this writing, gold is about \$633 per ounce.

Among the main bearish factors were: rumors of Iran's impending release of the American hostages [forecast in the last issue of *SGR*]; apparently false rumors of Iraq and Iran selling their gold reserves; uncertainty over the outcome of the US Presidential election; and profit taking.

There was also a \$500 million gold sale by the Soviet Union. After months of absence from the market, Russia had to sell bullion in order to finance needed grain purchases and carry out its imperialistic war on Afghanistan.

All of this triggered selling by technical chartists as a "descending triangle" broke out on the downside. And prices were pushed down even lower.

However, as we go to press, the market seems to be bottoming out in the low \$600's. The bearish factors appear to be pretty well discounted by now. The market may be poised to go up again.

For traders, we see short-term downside risk — with \$600 to \$610 as the first main support area and \$580 per ounce as the second, *and stronger*, support area. At this time, it appears that upside potential is greater than downside risk. But be cautious.

However, if you're a long-term buyer, holder, or hedger, this seems like a good time to buy, and increase the size of your holdings.

It is also noteworthy that during this period of extreme volatility in the gold market, silver gave up strength only grudgingly and within a very narrow range. This would seem to indicate silver's great fundamental strength as a long-term investment.

As SGR goes to press: October 24, 1980:

Latest Silver & Gold Prices

Comex spot contract: gold, \$632.50 per ounce;
silver, \$19 per ounce

London gold fix; a.m. \$628; p.m. \$633

Handy & Harman quote; silver, \$19; gold \$633

	Buy	Sell
1 ounce gold bar	\$ 633	\$ 657
\$1000 face value US pre-1965 silver coin bag	12,700	13,700
\$1000 face value US silver clad half dollar bag	4700	5500
\$1000 face value US circulated silver dollar bag	14,750	16,750
Gold coin in 10-coin lots		
Austrian 100 Corona	604	632
British Sovereign	160	190
Canadian Maple Leaf	639	657
Hungarian 100 Korona	602	632
Mexican 50 Peso Centenario	773	801
South African Krugerrand	644	662
US \$20 Double Eagle Liberty (uncirculated)	730	785
US \$20 St. Gaudens (uncirculated)	750	815

Coin and bar prices courtesy of Deak-Perera, New York.

