AMERICAN BASES IN GERMANY AND THE GOLD BASIS

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Germany is neither independent nor sovereign, prevailing pretences notwithstanding. It has American troops on her soil for reasons unexplained and unexplainable after all Soviet occupying troops were withdrawn almost 25 years ago. Equally significant is the fact that the lion's share of the German gold reserve is in American custody. If the Bundesbank asked for the repatriation of a token part of that gold over a long period of time, we may take it for granted that it was done on American instructions.

But why would the Americans ask the Bundesbank to request the return of a part of German gold from the 'safety' of the basement of the Federal Reserve Bank of New York in lower Manhattan? Surely not because the vaults are bulging with American gold and they have to make room for more.

It's all grand theater. There is a hidden agenda that has to be camouflaged. The best way of doing it is to put up a show. The public is fascinated by images of shuffling central bank gold.

One reason, perhaps the chief reason for this exercise is that the managers of the global fiat money system are preparing for the coming showdown, the final curtain on what some years ago I dubbed *The Last Contango in Washington*. In other words, policymakers are preparing for (or trying to fend off) permanent backwardation in the world's gold futures markets that is threatening to rip apart the present shabby make-belief payments system of the world.

Contango is the normal condition of the gold futures markets when the spot price of gold is at a discount relative to the price of futures contracts. It demonstrates that plenty of gold is available to satisfy present demand. People are confident that promises to deliver gold will be honored. The condition opposite to contango is called backwardation that obtains when the futures price loses its premium relative to the spot price and goes to a discount. In the gold market this condition is highly anomalous because, on the face of it, it allows traders to earn risk free profits. They sell spot gold at a premium, and buy it back at a discount for future delivery. However, risk free profits are ephemeral since the very action of traders will instantaneously eliminate them. What this suggests is that permanent backwardation in gold could never happen by the very nature of the case.

Yet unknown to the general public a very great danger is looming, the like of which has not threatened the world since the collapse of the Western half of the Roman Empire more than fifteen hundred years ago. This danger, should it materialize, would mark the end of our civilization and the beginning of a new Dark Age. I am talking about a threat of the sudden and complete collapse of world trade. It would be heralded by permanent gold backwardation, something that allegedly could never happen. Hard on its heels would follow the collapse of the dollar payments system. Barter, of course, would take place between neighboring countries, but world trade as we know it would disappear altogether.

The metric whereby the turning of contango into backwardation can be measured is called the *gold basis*. It is the premium on the price of gold for future delivery as per the nearby contract relative to the spot price. Thus negative gold basis is tantamount to backwardation. We have scarcely a forty-year history for the gold basis to go by, because there was no organized futures trading for gold before America defaulted on her international gold obligations on August 15, 1971.

Futures trading started out with a robust gold basis. Contango was at its peak. The gold basis cannot be higher than the full carrying charge (also known as the opportunity cost of holding gold, the major component of which is interest). But soon enough the gold basis started eroding, and erosion has continued to this day. This was an ominous process that was ignored by all politicians, economists and financial journalists.

The vanishing of the gold basis is all the more curious since it has been taking place against the background of a steady advance in the gold price. Textbook economics teaches that an advance in price always and everywhere calls out new supplies. However, textbook economics is helpless when it comes to gold. For gold the exact opposite is true: an advance in price makes supply contract; and a very large advance may make supply disappear altogether. The reason for this paradox is that gold is a monetary metal. All the bad-mouthing of gold by economists in the pay of governments won't change that fact. By now the decay has gone so far that the gold basis is practically zero, with occasional dips into negative territory.

Academia ostensibly avoids researching the gold basis, pretending that it has as much bearing on the world economy as the basis for frozen pork bellies. The public is kept in total ignorance. Yet you can ignore the gold basis only at your own peril. It is the only indicator available showing the progressive deterioration of the fiat money system. As is well known, there has never been a successful experiment with fiat currency in all history. Nor was it for lack of trying. Every such experiment was either abandoned as enlightened governments decided to return the currency to a metallic basis, or it ended in utter fiasco causing tremendous economic pain to people as the fiat currency was rapidly losing all its purchasing power.

The relentless contraction of the gold basis means that gold available for future delivery is fast disappearing. Gold is constantly moving into strong hands that hold on to it and will not relinquish it even in the face of steeply rising prices. Eventually the gold supply dries up and sporadic backwardation gives way to permanent backwardation. Gold mines refuse to take paper money for their product. If you want to have gold, you will have to have recourse to barter.

Permanent backwardation means that confidence in fiat paper currency and government promises to pay has evaporated. After all, considering their origin, irredeemable bank notes are nothing but dishonored promises to pay gold. Once confidence is shattered, all the king's horses and all the king's men cannot put Humpty Dumpty together again. Permanent backwardation is like a black hole. There is no way out of it. Not even a light ray can escape from its clutches. That's how black holes earn their name. 'Permanent backwardation' is not as suggestive as the name 'black hole', but it can gobble up the world economy nevertheless.

The gold basis is akin to the efficiency of bribe money. At first the bribe is taken with no questions asked. But as it becomes a regular feature of gold trading, effectiveness is lost. In the end the bribe is refused when it is realized that the objective is to cheat the holder out of his possession of gold. A trading system built on bribe is a house of cards. It is dishonest. It depends on deception and false-carding.

This brings me back to the German gold reserve. As sporadic backwardation in gold becomes ever more frequent, the gentlemen in charge of running the world's fiat money system get alarmed. The only way to pacify the market is to release more and more central bank gold. *Physical gold*. The beast must be fed. Paper gold will not do (although, of course, these gentlemen will keep trying to flood the market with it).

Releasing American gold to the futures market directly from the Fed is out of the question. It would confirm the suspicion, already rampant, that the dollar is a colossus of clay feet standing in knee-deep water. So let the client states of America do the releasing. The Germans have a reputation of favoring hard currency. They are reluctant to join the currencies' 'race to the bottom'. Germany is the natural choice to feed the gold futures markets in an effort to protect the dollar against the last assault that is shaping up.

For a long time America has been twisting the arm of other countries, including the U.K. and Switzerland, making them sell hundreds of tons of central bank gold, while America was not selling one ounce. "Do as I say, not as I do!" During all this time Germany was not selling either. The appearance was maintained that this decision was made in Germany. It wasn't; rather, it has the mark "made in U.S.A." German gold is the last defense of the dollar. By now practically all central banks ignore the siren song from America. From sellers they have become buyers of gold. According to the American master plan Germany is the last fort of the crumbling global fiat money system. Germany will not defect: that is the purpose of keeping American troops on German soil. Germany will dutifully do the job of feeding the futures market with gold in an effort to fend off permanent backwardation. The repatriation of a part of the German gold reserve is a trial balloon. If markets get scared and panic selling occurs before the Bundesbank starts selling, so much the better. But if false-carding fails and the world-wide

march of gold into private hoards continues unabated, then let the Bundesbank, not the Fed, bleed gold. America's gold must be spared at all hazards.

On such tricks and deception is the international monetary system grounded.

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What, then, is the solution? How can sudden death in world trade be averted? Fortunately, there are still upright politicians around. Godfrey Bloom of the European Parliament, MP for Yorkshire and North Lincolnshire ridings in the U.K. suggests that *Germany should repatriate ALL of its gold and reinstate a golden deutsche mark.*

The underlying cause of the world financial crisis is runaway debt. Gold is the only *ultimate* extinguisher of debt. Since its expulsion from the international monetary system total debt in the world can only grow, never contract. To stop the cancerous growth of debt gold must be reinstated in its former position as the guardian of the quality of debt.

If, defying American wishes, Germany took the initiative in creating a gold mark and opening the German Mint to gold where all comers could convert their gold ingots into gold coin, the course of world history would be changed. *It would be Germany's finest hour.* Civilization will have been saved and the onset of a new Dark Age averted. The gold mark could circulate side-by-side with the irredeemable euro and dollar. Let the people decide whether they want to get paid in crisis-prone fiat currencies or, perhaps, they prefer the time-honored stability of the gold coin. It is hardly in doubt what the choice of the people would be.

The German initiative will set off a chain reaction of similar virtuous acts by the major central banks of the world, in order to prevent the fatal depreciation of their currencies against the gold mark. The latter will be well on its way to become the most coveted currency in the world for international trade. The financial system will be saved from the ordeal of competitive currency devaluations and from the corrosive effect of ever-expanding government deficits. Governments will be forced to face reality and live responsibly within their means like everyone else.

Farmers will no longer be paid for not farming, and able-bodied workers for not working. Youth unemployment, in particular, will be a thing of the past.

There is a precedent. In 1948 Germany defied the occupying force when it created the Deutsche Mark without bothering to ask for permission in Washington.

But is the gold standard not deflation-prone? In the 1930's the international gold standard collapsed because of this very fact, did it not?

As the father of the Deutsche Mark, Wilhelm Röpke (1899-1966) said: *it is not the gold standard that failed, but those in whose care it was entrusted.*

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