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GOLD BASIS SCREWED

Who needs a thermometer to know that the heat-wave is on?

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Fofoa has just published another thoughtful paper with the title: *Red Alert: Gold Backwardation!!!* http://fofoa.blogspot.com. It raises the question nobody has apparently raised before: "Is the dollar bidding for gold, or maybe gold is bidding for dollars?" And it gives an amazing answer: the gold basis has been screwed and it has been giving bogus signals for more than a year. We have likely had backwardation all this time but it has been stonewalled. There is no real gold market any more. *Goldman Sucks is playing with itself*. Most trades are bogus, sales as well as purchases. Leases ditto. What Goldman Sucks couldn't get away in a falling market, it can in a rising one.

There are other metrics beside the gold basis that the market has developed in the meantime. One such is GOFO = $ LIBOR – GLR (the gold lease rate). On the face of it, GOFO cannot ever go negative. If it did, it would mean that the risk in borrowing gold is greater than the risk in lending dollars, even though the latter has infinite counterparty risk. But there is no counterparty risk in borrowing gold! That's a telltale for you. Nasty negative GLR, nasty negative GOFO, shut up, both of you!

Fofoa says that the dollar needs voluntary bids from private physical gold holders to survive. But the pool of *real* bids is bone dry and cracking. Dollar liquidity is just a cheap façade. As the gold price rises slowly, nervous Nellys, suckers, and other weak hands will relinquish bits and pieces of the yellow precious which will keep the merry-go-round in motion. Gold-bidding for dollars can be kept alive on a life support system. Indefinitely? Pretty well. But Fofoa says that Goldman Sucks has shot itself in the foot.

I can add little to these speculations, but I would like to note another telltale: the fine Goldman Sucks has agreed to pay Uncle Sam. On July 19 The New York Times carried a story entitled: *Goldman Employee Denies Fraud*. Just days after Goldman agreed to pay $550 million to settle securities fraud claims, a midlevel employee of the bank, Fabrice Tourre, has filed a 13-page denial and sought dismissal of the case. Smell the stink? Goldman agrees to pay more than half a billion while a vice president, central to the case, challenges the charges. To add another little twist, according to the NYT article, Goldman Sucks released a batch of old e-mail messages of Fabrice Tourre, who calls himself "Fabulous Fab" for his skills in selling "Frankenstein bonds" (= bonds going bad fast) "to widows and orphans" on the tarmac of Brussels airport, designed to damage Mr. Tourre's case in the continuing S.E.C. investigations.

Who is fooling whom here? Is it possible that the fine they levy and pay is just another case of check-kiting? But why would they do such a thing? Why, a bogus fine could deflect suspicion away from a much bigger charade in misleading the public, namely, to cover up goldbackwardation!

Meanwhile all we can do is to sharpen our tools in sleuthing to uncover the contango. I started a Seminar in Australia in 2008 on backwardation and the secular vanishing of the gold basis. By all standards, it was a huge success. We continued in 2009 and were making plans to reassemble in Sidney, Australia this year in November. I am sorry to give notice that the 2010 The Third Annual Seminar on gold backwardation and the last contango is cancelled, due to the greed of the professional organizers of the event. Rest assured, however, that the research is going on, and if we get a decent invitation, we shall make up for the cancelled event, with further revelations!

In the meantime, here is a hint to whet your appetite. Fofoa should refine his indicator GOFO as follows. GOFO = LIBOR – GLBR, where GLBR = gold lease *bid* rate, i.e., the rate which bidders are willing to pay for leased gold to the bullion bank. It should be somewhat greater than GOFO as it has been defined up to now. (Why?) It is true that GLBR is not publicly quoted, but a little bit of sleuthing should be able to produce a proxy. Then GOFO will tell you how profitable the gold carry trade is, or is getting. Negative GOFO tells you that it is making a loss and net shorts in gold are under water or will soon be.

But there is another indicator equally important for successful sleuthing. (Goldman Sucks, are you listening?) I shall call it COGOFO. Here it is: COGOFO = LIBBR – GLOR. Here LIBBR = London interbank *bid* rate; it is the rate at which a bank in the London market is willing to borrow from another. Furthermore, GLOR = gold lease *offered* rate; the rate at which bullion banks are willing to lease out gold. Again, LIBBR is not in the public domain, so due diligence is required to come up with a reasonable proxy.

Here are some quiz questions: (1) What is the relation between LIBOR and LIBBR (2) and between GLOR and GLBR (3) and between GOFO and COGOFO? (4) Can COGOFO go negative, and if so, what does it mean? (5) How can you make inferences about movements at large between cash gold and paper gold from the variation of GOFO and COGOFO? (6) If you plot GOFO and COGOFO, what does a crossover of the two mean?

As my faithful students will notice, the distinctions I am recommending to Fofoa are those of Carl Menger, the 19th century founder of the Austrian School of Economics. The New Austrian School of Economics that will start its first ten-day course on August 9 in Budapest will provide its audience with full background on Menger's theories, and how to apply them in the present situation where markets are rigged and governments are lying. Send in your answers to: aefekete@hotmail.com, and participate in the draw that will take place at the 3rd Australian Seminar on Backwardation and the Secular Vanishing of the Gold Basis! Prizes will include gold nuggets.

IMPORTANT ANNOUNCEMENT

Thanks to a recent donation, scholarships covering tuition and college accommodation at the ten-day course (see below) have become available for students. First come, first served.

Calendar of Events

THE ESTABLISHMENT OF THE AUSTRIAN SCHOOL OF ECONOMICS IN BUDAPEST. The first ten-day, 20-lecture course offered is entitled: Disorder and Coordination in Economics — *Has the world reached the ultimate economic and monetary disorder?* The lecturer is Professor Fekete, with the cooperation of Mr. Rudy Fritsch (Canada), Peter van Coppenolle (Belgium), and Mr. Sandeep Jaitly (United Kingdom). It will be held in Budapest, Hungary, from August 9-20, 2010. Participation is limited, early registration is advisable. For more information and registration, contact Dr. Judith Szepesvari at: szepesvari17@gmail.com. Inexpensive dorm-type accommodation is available for students (shared bathroom, shared kitchen); a three-star hotel is next door. Extra-curricular consulting with Professor Fekete can be arranged for an extra fee.

The school is meant for all students (including beginners) interested in the real answers to the present economic crisis and misery. Its program plans to cover the whole spectrum of Austrian economics, with special emphasis on developments that took place after the death of the greatest 20th century economist, Ludwig von Mises, including the Real Bills doctrine and social circulating capital; the theory of money, credit and banking; and the theory of interest and discount.

Completion of this course will earn participants one credit towards a four-course, four-credit program that has been submitted for accreditation to the Adult Education Accreditation Board of Hungary. Participants will receive a certificate signed by Professor Fekete. The follow-up credit courses will cover these areas:

Adam Smith's Real Bills Doctrine and Social Circulating Capital.

The Austrian Theory of Interest and Discount.

The Austrian Theory of Money, Credit, and Banking.

Some of the future courses may be offered in Martineum Academy in Szombathely, Hungary, where we have had four successful conferences already in the past. A special cordial invitation is extended to all Martineum alumni and their family members and friends!

Eating and shopping facilities, as well as a swimming pool are nearby. Spectacular excursions can be arranged in the surrounding hills, and boat trips on the River Danube.

It is well-known that Budapest is one of the foremost spas in Central Europe with a dozen or so medicinal thermal springs. Participants of the course could stay on afterwards and savor the superb spa and cultural offerings in the city. Make it a family holiday!

Meeting in Hong Kong

We have plans for a two-day meeting in Hong Kong and another neeting in New Zealand in November, 2010. Stay tuned for further announcements.