The Silver Saga

What says the silver with her virgin hue?
"Who chooseth me shall get as much as he deserves."

(Shakespeare, *The Merchant of Venice*)

THE INCREDIBLE COLLAPSE OF VALUE OF SILVER IN THE 19TH CENTURY

– DON'T BLAME COMSTOCK! –

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An Address Delivered at the Conference Held at the University of Padova
on November 30, 2012
*"Coin Finds and Historical-Economic Processes in the Ancient World:
Ten Years of Research 2002-2012"*

The silver standard did not die a natural death. *It was deliberately killed*. A proper search for the assassins was never carried out. There was never a *post-mortem.* In this paper we focus on the conspiracy as it might have unfolded between the two dates: April 9, 1865 (the day General Lee of the Confederacy surrendered at Appomattox to General Grant of the Union marking the end of the War Between the States) and January 1, 1879 (Resumption Day, when payment of the victorious Union's currency, the greenback was resumed in gold specie – *but not in silver*).

China has been on the silver standard since time immemorial. The Chinese did not use coins for monetary purposes such as bank reserves until the end of the 19th century; they used the *sycee*, a shoe-shaped ingot of approximate size 5×3×3 inches, weighing approximately 50 taels or about 5 pounds (avoirdupois). No one can pretend to know, however approximately, how much monetary silver has gone into hiding in China and in India, these two most populous countries also known as the world's sink for silver, over the millennia. In comparison estimates of monetary gold having gone into hiding over the same period of time are far more reliable. Be that as it may, the amount of monetary silver unaccounted for is probably greater than any estimate ever made.

In the 19th century silver coins did most of the money-work in the world. The *turnover of silver coinage* (the value of silver coins times their velocity) was at an all-time high, eclipsing the turnover of gold coinage by far. Inept governments did not follow the lead of Isaac Newton, and they tried to enforce a rigid exchange rate between the two monetary metals (called the Mint ratio). This system was called *bimetallism* – a stillborn idea.

Bimetallism destabilized the natural monetary system based on silver and gold valued at a *variable* rate, as Newton's monetary system in Britain did. Bimetallism was the disease, the demise of the silver standard was the unfortunate consequence. In the Western countries by 1879, in India by 1893, in China, the last stronghold of silver, by 1935, silver was demonetized. Between the two dates 1879 and 1935 *the world witnessed a most spectacular event: the collapse of the value of silver by more than 80% in a little over half of a century.* Silver fell from $1.29/oz in 1873 to 25¢/oz in 1935. Putting it differently, the gold/silver price ratio rose from 15:1 to more than 80:1. Never in history, ancient or modern, have markets put such fancy values on gold in terms of silver.

Who killed the silver standard?

All this can be neatly explained in terms of the Quantity Theory of Money. The richest silver vein ever, called the Comstock Lode was discovered in Nevada in 1858. Surplus silver inundated the economy and lost most of its value due to the oversupply and the lack of matching demand.

But this explanation will not satisfy those of us who consider the Quantity Theory of Money as a mere mechanical metaphor. As a theory it is bound to fail because it is trying to give a linear explanation of highly non-linear phenomena. January 1, 1879, Resumption Day, when the payment of the greenback in gold (but not in silver) specie was resumed, coincided with the date when the Latin Monetary Union in Europe closed its last Mint to silver – marking the end of the silver standard in the Western countries. The coincidence is ominous.

No satisfactory explanation has been offered in the literature for the fact that the closing of the Mints to the free coinage of silver was the starting point of an unprecedented destruction of wealth world-wide, due to the relentless fall in the price of silver during the following 55 years. To make matters worse, it was destruction of *liquid* wealth. Not only did silver lose more than 80 percent of its purchasing power; it also ceased to be a monetary metal. As a consequence, silver became so much harder to sell. Worse still, the steadily falling price caused panic-mining of silver. Miners were anxious to sell before the price fell even more. As a result, almost all silver mines were mined out prematurely. Thereafter all silver output came as a byproduct of mining other minerals. These effects compounded and made the destruction of monetary values, that is deflation by another name, so much worse.

The collapse of the silver price was a major historical event affecting the entire globe and all trading nations of the world. It caused the impoverishment of the indigent classes in India, China, and elsewhere in Asia. But it also wiped out the credit-worthiness of the middle classes in Europe that lost their landed wealth as a consequence. Monetary historians failed to treat this aspect of the demise of the silver standard with the seriousness it deserved. They also misdiagnosed the deflationary bias that the monetary system showed in the first half of the 20th century. The gold standard that arose on the ashes of the old monetary order in the wake of the destruction of the silver standard was less than satisfactory. Silver demonetization has made all hoarding demand fall upon gold. This imparted a deflationary bias to the international gold standard that enemies of sound money were able to exploit with all consummate skill.

Following a vicious campaign of anti-gold agitation gold was also demonetized by the governments exactly one hundred years later, in 1973. The demonetization of gold was no less unconstitutional than that of silver a hundred years earlier. It was also based on chicanery for good measure.

It should be noted that *hoarding gold and silver is not an aberration*. It is, in fact, part of the essential mechanism regulating the rate of interest. It will bar the banks from suppressing interest. When depositors realize what the banks are up to, they withdraw their deposits in the form of gold coin. The banks lose reserves and are forced to call in loans. It will also act as a deterrent against government profligacy. Ordinary citizens become disturbed by the government's overspending and serial budget deficits. In response they show a preference for holding their liquid wealth in gold coins instead of short-term government paper. Such hoarding demand previously fell upon gold as well as silver. Now it was falling upon gold exclusively. The deflationary consequences are obvious.

One instinctively feels that there is no way self-destruction of liquid wealth of so great a magnitude could occur spontaneously in such a short space of time. The event could not be explained on the strength of causality. We must invoke teleology if we really want to understand it. Such an analysis was never carried out. Furthermore, speaking of *destruction of wealth* is not quite accurate. Value was not destroyed in the same sense of a house burning to the ground.

Clandestine embezzlement

Rather, it looks like a clandestine embezzlement to benefit the world's banking establishment at the expense of account holders. Their assets were manipulated downwards in value and ultimately taken over by the bank. The perpetrators were not worried that the disappearing liquid wealth would be missed and cause deflation. That was just the point of perpetrating it. They were confident that if they replaced the disappearing silver with bank credit based on debt, in particular, the debt of the government, then there would be no deflation. This strongly suggests government involvement. In all probability there was a conspiracy between an international banking cartel and some governments (e.g., the United States government acting either alone or in connivance with Imperial Germany).

Economic historians describe the Silver Saga as a natural evolution whereby gold monometallism gradually displaced bimetallism while strangling the silver standard. According to this reading of history, the market gradually eliminated silver as money, as it has so many other challengers of gold's supremacy in the race for monetary hegemony beforehand. It was destiny. No need for a *post mortem*, still less for a search for the assassin. What would happen if every death due to natural causes was investigated as if it was due to violent causes? At any rate, they claim, the Quantity Theory of Money fully explains the market process eliminating silver from monetary circulation.

Upon closer examination the hypothesis that it was the market rather than collusion between governments and banks that killed the silver standard appears untenable. There were powerful pressure groups pushing for the closing of the Mint to silver. One such pressure group representing special interest was that of international banking houses — given their well-known penchant for monopolies. They avoided public debate. They acted behind the scenes. A monopoly of the gold standard would mean, for them, a better handle on money-creation through their control of the gold mines, as well as their control of public credit. If this hypothesis is correct, then we know what sealed the fate of the silver standard.

Whodunit?

Prussia was victorious in the Franco-Prussian war of 1870-71. The German Empire was proclaimed at the Palace of Versailles on January 18; Paris fell to the invading German troops on January 28, 1871. Germany was anxious to join the gold standard club led by Britain. On November 23, 1871, Bismarck exacted a reparation of five thousand million gold francs (or one billion gold dollars, or 200 million pounds) from France payable in four years. Northern France was to remain under German occupation while the full amount was settled. Arguably this was the largest amount of gold ever changing hands directly, without involving promises to pay. One thousand million dollars in gold (at $19.39/oz!) is an incredibly huge sum of money by any standard. In comparison, the Lousiana Purchase in 1803 was consummated for a total sum of $15 million in gold. The Alaska Purchase in 1867 was consummated for $7.2 million in gold. This makes the French indemnity to Germany equivalent to 66 Louisianas or 172 Alaskas.

The temptation for the Germans to increase the value of their gold booty by fair means or foul may have been irresistible. For example, it could be increased by demonetizing silver. That would increase the demand for, and so also the purchasing power of gold.

France paid the indemnity ahead of schedule. The new gold standard of the German Empire was inaugurated on July 9, 1873, when the new gold coin, the gold mark made its debut. This was preceded by closing the German Mints to the coinage of the silver Taler in 1871, the first overt step towards demonetizing silver.

Some historians maintain that the demonetization of silver and the subsequent sale of melted coins by the German government on the world market was the direct cause of the precipitous fall of the value of silver. However, this is flatly contradicted by the fact that on February 12, 1873, the day when President Ulysses Grant signed the Coinage Act of 1873 into law, *silver fetched a higher price in the market than the Mint price*. No silver was flowing to the Mint. Records of the minting of the standard silver dollar show that there has been no demand for the monetization of silver on private account. This situation continued for some time afterwards. Silver mines continued selling their output on the free market. They seem to have been unaware that silver had been effectively demonetized by Germany in 1871 and by the United States in 1873. It made no difference to them: the market offered a better price.

The ultimate damage to the price of silver was *not* inflicted by German demonetization. Nor was it inflicted by demonetization in the United States. The market knew that demonetizations were coming and took them in stride. There was a ready market for silver in India and China, presumably for any amount, however large. American silver miners started to look at the U.S. Mint as a potential market for their production in 1875, as the price of silver in terms of the greenback was weakening. They were shocked to find that the Mint had been closed to silver years earlier.

The anatomy of a murder

Here is the step-by-step chronology of the passage of the bill that was to become the Coinage Act of 1873. It eliminated the standard silver dollar by default, in failing to mention it. This removed the authority to mint any more. *The removal was unconstitutional.* Since that coin was the only silver coin that could be struck in unlimited amounts for private account, it also meant the demonetization of silver by the United States of America, following the example set by Germany.

(1) In 1868 senator John Sherman of Ohio sponsored a bill that, among other things, proposed that the Mint be closed to the coinage of the Constitutional silver dollar, thus demonetizing silver in the United States. Although there was no opposition, the bill died in committee because the Senate was busy with other things, such as the greenback inflation struggle. Note the early date 1868!

(2) Secretary Treasury Boutwell sent the bill (that was to become the Coinage Act of 1873 omitting the standard silver dollar) to Congress on April 25, 1870 with his strong recommendation for passage.

(3) The Senate passed the bill on January 10, 1871 by a vote of 36 to 14. Among the *ayes* were the two senators from the silver state of Nevada. (At the time Nevada was the only silver state as it had been admitted to the Union in 1864. Colorado was the second admitted in 1876, followed by Montana, Idaho and Utah admitted between 1889 and 1896).

(4) The House passed the bill on May 27, 1872, by a vote of 110 to 13. Support among representatives from the silver state of Nevada was again overwhelming.

(5) President Grant signed the bill into law on February 12, 1873. It is important to note that all the details, including the entire text of the bill, were in the public domain as early as April, 1870.

25 years later, in 1895, Senator John Sherman, who was the sponsor of the bill in the Senate, in a famous speech of his entitled *On the Crime of 1873* stated that, while the bill was pending in Congress for as long as three years,

> "it was carefully considered in both houses and special attention was called to the omission of the standard silver dollar, and for the reasons for this omission… It is strange that the very men who supported and urged this coinage law of 1873 and demanded the exclusive coinage of gold are the very men who now [in 1895] demand the free coinage of silver…

Later in that speech Sherman related that his colleagues, Senators Jones and Stewart of the silver state of Nevada, were

> "urgent and honest in saying that gold was the best and only standard of value". However, they changed their minds when production from the Comstock Lode in Nevada [discovered in 1858] increased greatly, and the first signs of weaknesses in the silver price started to show after 1874. Then they wanted a market for their silver. They wanted themselves and their friends to pay existing debts and obligations, that had been contracted on gold basis, in silver; but took care in their own contracts to stipulate that debts owed *to them* were payable in gold." (*The World's Famous Orations: John Sherman*, http://bartleby.com)

Smoking gun

In 1873 neither silver nor gold coins circulated in the United States, although the Mint was open to both metals. The country was on the 'greenback standard': irredeemable paper money issued by the Union to finance its efforts in the War Between the States, which circulated at a discount of about 13 percent to silver. It was understood, however, that gold payments on the notes would be resumed (as indeed it happened on January 1, 1879) and the greenbacks would ultimately be withdrawn from circulation pursuant to the Resumption Act of 1875. The question whether resumption was to be extended to silver payments as well was bypassed in silence.

The prospect of resumption could be the smoking gun prompting the international banking houses to commit the crime. On April 9, 1865 (the day of Appomattox) an incredible opportunity to grab and usurp monetary powers presented itself. Obviously, *resumption was coming, followed by a great increase in demand for gold and silver. This could be exploited most effectively for private gain if silver could somehow be eliminated as a monetary metal. The thing to do for the banking houses was to initiate an arbitrage operation of selling silver-mining shares against buying gold-mining shares in anticipation of the demonetization of silver.*

Such an operation would take a number of years. By 1873, eight years later, following the German Empire, silver also had been demonetized in the United States through the back door, so to speak. Of course, speculators would start dumping silver in large quantities and selling it short, causing the price of silver to fall precipitously as early as 1868, when Senator Sherman spilled the beans in proposing the demonetization of silver. That never happened, making the whole affair very suspect. The evidence appears to suggest that, far from being 'an honest mistake', the omission of the standard silver dollar from the Coinage Act was a deliberate act to destroy individual property rights – possibly in collusion with Germany.

These two parvenu countries might have wanted to get the best mileage out of their respective victories in the battlefield. The indemnity of one thousand million dollars in gold exacted by Germany from France would be that much more valuable, in view of the falling commodity price level in terms of gold. On the other side of the water the banks could greatly enrich themselves by making the mortgages on land in the former Confederacy, assets that they now controlled and which had been denominated in silver, payable in gold. The extra value would come out of the hide of the victims of the War Between the States. The coincidence of interest of the two countries is telling. The would-be perpetrators of the crime had reasons to make speculators behave differently from the norm.

Circumstantial evidence

The banking houses in the United States were apparently playing a duplicitous role. As observed above, there was a possibility for profitable arbitrage in the market for mining shares. The banks would bet against silver while getting ready to profit from a prolonged decline in the price of silver afterwards. *It was not in their interest that the decline start immediately.* They needed time, possibly years, to complete their arbitrage operations in mining shares. They wanted to get rid of their silver mining shares and replace them with gold mining shares. It is a plausible assumption, therefore, that the banks temporarily supported the price of silver (which they would have to do in the normal course of their business anyhow) but with the ulterior motive of preparing for the final assault on the silver price later. They succeeded in fooling the speculators not to place their bets against silver.

If the demonetization of silver was not the result of a long-term market process (as suggested by virtually all economists) then the question is: what was it the result of? This question has never been answered satisfactorily. My answer is that *it was the result of the collusion of banks to manipulate the silver and gold market secretly, and carefully coordinating it with their manipulation of the market for mining shares.*

Leads and lags

To prove my theory I worked out a research program. It involved compiling the daily closing prices of eight series as follows:

(1) asked price of silver
(2) bid price of silver
(3) asked price of gold
(4) bid price of gold
(5) average asked price of silver mining shares
(6) average bid price of silver mining shares
(7) average asked price of gold mining shares
(8) average bid prices of gold mining shares

in the United States for the ten-year period from 1868, the year when the idea of demonetizing silver first surfaced in Senator Sherman's committee, to 1878, the year when the Latin Monetary Union decided that the silver price has been mortally wounded, was beyond hope of recovering, and closed its last Mint to silver.

From the eight price series above one can obtain four series of key price-spreads by taking differences as shown by tabulating them in the following table:

PRICE-SPREAD SERIES

series	arbitraging	
(4) minus (1)	from gold	to silver
(3) minus (2)	from silver	to gold
(8) minus (5)	from gold-mining shares	to silver-mining shares
(7) minus (6)	from silver-mining shares	to gold-mining shares

Next, one calculates the standard deviation from the means for each of the four price-spread series. By well-known theorems of mathematical statistics the standard deviation filters out 'noise', that is, random causes of price variations, but catches singular irregular causes (e.g., discovery of a major gold or silver ore deposit or, most especially, concentrated efforts to manipulate prices).

One is looking for leads and lags. In particular, if arbitrage from silver-mining shares to gold mining-shares did lead arbitrage from silver to gold, and the latter did lag the former, then this would *not* be a random event. It would be conclusive proof that arbitrageurs were acting in unison to bring about a collapse of the silver price for maximum private gain.

When I wanted to carry out my research project, I found that it was beyond my meager resources. Rather naively I assumed that most of the work had already been done, some of the price series had been compiled and some of the standard deviations from the means calculated. The collapse of the silver price after 1875 was so spectacular, it was such a precipitous and momentous event, involving the international monetary system, the wealth and welfare of so many people, literally changing the course of history, that some researchers at least could have questioned the 'conventional wisdom'. They could have rejected the market-process hypothesis. These researchers should have started looking for evidence of active connivance between governments and banks during the intervening 140 years. This, however, does not appear to be the case. Everybody without exception has accepted the pat explanation for the silver price collapse in terms of the Quantity Theory of

Money. Yet it is possible that 1875 marks the year when the conspirators completed their program of arbitrage from silver mining shares to gold mining shares; and started their follow-up program of arbitrage from silver to gold. It is not impossible to find out the truth about it some 140 years later.

Researchers of today would have to start from scratch. This is a task I can no longer undertake, in view of my advanced age. But I would certainly encourage the younger generation to do it. I hope that my tentative research plan is going to be helpful to them. I have no doubt whatsoever that this would be a worthwhile project.

I call attention once more to what above I have called 'circumstantial evidence' of monetary mischief. In the absence of mischief the silver price ought to have started its descent much earlier, several years before 1875 – possibly as early as 1868. Speculators (as distinct from bankers) must have been watching the political wrangle over silver starting in 1868. It appears that *speculators missed their opportunity to sell silver short*. This would be rather uncharacteristic of their trade, an assumption we can safely dismiss. A more plausible assumption is that the conspiring bankers met the speculators' short selling head-on. *They bought silver*. As pointed out already, they needed time to complete their program of arbitrage in the mining-share market for monetary metals. Once it was completed, after they have sold their quota of silver mining shares and bought their quota of gold mining shares, they would be the first to dump their silver and let speculators do the rest. Of course, the duplicity of their conspiracy makes the detective work so much harder.

Monetary mischief

There is no doubt that the U.S. Congress grossly exceeded its authority when it passed the Coinage Act of 1873. In signing it President Grant shared responsibility for making the unconstitutional bill the law of the land. The Act nowhere mentions the Constitutional standard silver dollar, the only coin cited by the Constitution – as if no such coin has ever existed. Consequently the interpretation arose that there was no authority for coining it by *anyone* after the Act became law.

The contrast with the logical interpretation of the Constitution is striking. According to the Constitution the standard silver dollar can be minted in *unlimited quantities* for the account of anyone tendering the silver to the Mint. Not only is the standard silver dollar to serve as a yardstick but, even more importantly, it is there to test the *material*, silver, out of which the yardstick is made. If you eliminate it or obstruct its availability, then the standard silver dollar obviously cannot discharge that function. It makes no sense to tie the access to it to permission from Congress, from the President, from the Secretary of the Treasury, or anyone else. In legal matters the Constitution takes precedence until amended. This is a clear case of usurpation of powers. *The standard silver dollar had to go because the public was to be deprived of a means to test the monetary quality of silver.*

The Constitution guarantees the right of the individual to take silver to the Mint in unlimited quantities. Only in this way can we be certain that silver is sufficiently inelastic to serve as the yardstick of value. If the flow of silver to the Mint was orderly, then the yardstick would be satisfactory. But if the Mint were inundated with silver and could not be kept open for that reason, it would be proof that silver was no longer suitable to serve as material out of which the monetary yardstick could be made. It would show that silver had a rubber-like quality: it was much too elastic. It would show that silver has failed the test. It hasn't got the quality every monetary metal must have: the quality of having constant value.

As a matter of historical record silver has never been put to the test. There has *never* been a run on the Mint by owners of silver bullion wanting to turn their metal into silver coin before it was too late. In every instance the run on the Mint occurred, it was not because people feared that the price of silver would collapse. It was *because inane government policies made silver-to-gold arbitrage risk-free.* People bought silver abroad in exchange for melted U.S. gold coins. They wanted to get more gold coins at the U.S. Mint for their silver – as was their right to do under bimetallism. Then they wanted to export the gold coin, since it was worth more abroad, and they wanted to continue this arbitrage indefinitely for the risk-free gain it afforded them.

When the Mint was closed to silver, it was a protective measure taken by the government in trying to prevent further losses to its gold reserve. *It was not a failure of silver*. *It was a failure of bimetallism*. The solution was not the demonetization of silver: it should have been the abolition of bimetallism.

Conclusion

I have never been a conspiracy theorist. I never joined latter-day crowds crying "stop the manipulation of the silver and gold price by unlimited short sales!" I know full well that the present low price of silver is a remnant of the tragic outcome of the Silver Saga that started some 145 years ago at Appomattox. The prospect of Resumption of specie payments after the War Between the States created an incredible opportunity for monetary mischief. The circumstantial evidence is that the opportunity was fully exploited by an international banking cartel to sabotage the international monetary system. This observation does not make me a conspiracy theorist. I am offering a detailed plan to find out, some 145 years after the event, using the method of standard deviations from the means borrowed from mathematical statistics. We owe it to ourselves to do the necessary research. The world economy, sagging as it is under the weight of its debt tower and fast depreciating irredeemable currencies, is clearly on its way to self-destruction. The forcible elimination of, first, silver and then a hundred years later of gold, from the monetary system removed the only ultimate extinguishers of debt we have. In consequence, total debt can only grow, never contract. The process is hidden since the unpaid and unpayable debt is accumulating as sovereign debt of governments. The world is deluding itself that sovereign debt can increase indefinitely as governments can extend its maturity indefinitely. In 2008 we had the wake-up call that it cannot. Unless we stop the proliferation of debt, the world is facing prolonged deflation, depression, continuing capital destruction, bankruptcies and unprecedented unemployment. It is leading to a breakdown of law and order. It could spell the end of our civilization.

Note. A fuller version of this address is posted on my website www.professorfekete.com under “Scholarly Economics”.