Chapter 6 – The Big Reset

New rules have been discussed not only inside the advanced economies, but with all emerging economies, including China.

– Jean-Claude Trichet, former president of the European Central Bank

Politicians in Washington have done nothing substantial but postpone once again the final bankruptcy of global confidence in the US financial system.

– Xinhua

With the status of the US dollar as the international reserve currency being shaky, a new global currency setup is being conceived.

– Zhou Ming, General Manager of the Precious Metals Department ICBC

The world is moving step by step toward a de facto Gold Standard, without any meetings of G20 leaders to announce the idea or bless the project.

– Ambrose Evans-Pritchard, international business editor, The Telegraph

I believe that basically the system is broke[n] and needs to be reconstituted. The system we now have has broken down, only we haven't quite recognized it. So you need to create a new one and now is the time to do it.

– George Soros, hedge fund manager

INTRO

The world economy and its currency system can be compared to supertankers. All route changes have to be planned well in advance. If history has taught us anything, it is that a currency tends to lose its world reserve status over a long period of transition. The 'endgame' is often drawn out over decennia. The British pound first suspended its gold standard at the start of World War I in 1914, but it was not until 1944 that the dollar became its successor (during the last Big Reset).

Although the US understands that the dollar will one day lose its world reserve currency status, the Americans will try to maintain their monetary supremacy for as long as possible. Actually, it was already apparent to the Americans back in 1971 that the endgame for this dollar-based system had begun. For over 40 years, the US has used all its power, creativity and flexibility to keep its monetary allies on board. Every trick in the book has been used to convince countries to support the dollar and to marginalize the role of gold.

But since the Fed has started to monetize most of the newly issued debt as part of its QE operations, the point of no return has been passed. Probably even within the next decade, the global financial system will have to find a different anchor. We can expect the US to take the initiative again before a real crisis of confidence occurs.

79. Why do you expect a Big Reset of the global financial system?

Our financial system can be changed in almost any way as long as the main world trading partners can agree to the changes. There are two types of resets: those that are planned well in advance – such as the Bretton Woods reset in 1944 which affected almost the whole world – and smaller resets needed due to monetary developments. Examples of the latter are the introduction of the gold-backed D-Mark after the Weimar hyperinflation in 1923 in Germany, the closing of the gold window by the US in 1971, and the theft of depositors' money during the rescue of the Cyprus banking system in 2013.

Two major problems in the world's financial system have to be addressed: 1) the demise of the US dollar as the world's reserve currency, and 2) the almost uncontrollable growth in debts and in central banks' balance sheets. For all of these issues, central banks have only been buying time since the start of the credit crisis in 2007. Insiders predict that much more radical action will be needed before 2020.

In 2013, the Chinese openly said that the time had come to 'de-Americanize' the world. They called for 'the introduction of a new international reserve currency that is to be created to replace 'the dominant US dollar'.[274] The Chinese have been studying how a reset could occur for quite some time.[275]

But given how sensitive this issue is, nothing can be said in public. Any official comments about a new 'Plan B' will crash financial markets (Plan A) immediately. Central planners know the only way to plan a reset is to do it in total secrecy. That is why investors have to watch what central bankers do instead of what they say and prepare themselves well in advance.

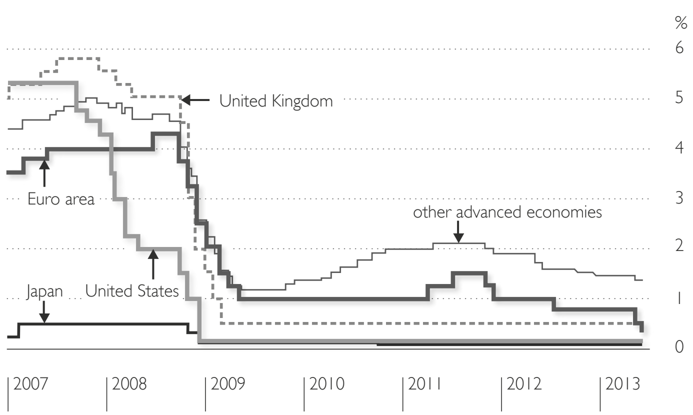
274 http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aeFVNYQpByU4

275 Reserve Accumulation and International Monetary Stability, 13.4.2010, http://www.imf.org/external/np/pp/eng/2010/041310.pdf

Many monetary reforms, like the one in Cyprus, are executed on the weekends when financial markets are closed. On many occasions, there are no concrete warning signs. Only insiders and their 'smart-money' (i.e., hedge-fund) friends tend to be positioned well in advance.

But one thing is certain: in almost all monetary crises and resets, holders of (physical) gold (and silver) have come out financially unharmed. This is because 'gold is nobody's liability'. China stopped buying US Treasuries in 2010 and has been loading up on gold ever since, which is a sign not to be ignored. The Russians have been aggressively buying gold as well, ever since the start of the credit crisis in 2007. The fact that the US is still fighting gold with everything in its power is a clear indication that gold will probably be an important part of a planned reset. If not, it will at least be the best safe haven when the storm passes.

Policy rates advanced economies



Source: BIS

80. How can the international monetary system be changed?

Most people see our financial system as a binary system with only two options: it will work (0) or it will crash (1). They tend to forget that this is a highly flexible system, which can be adjusted in many ways. Because the current system is constructed by mankind and does not follow the rules of natural law, almost any desired change can occur.

In theory, all debts worldwide could be wiped out on a Sunday afternoon. We could start from scratch with a new balance sheet the next morning. If every citizen in the world was to be credited with let's say 1,000 newly designed Bancors, which would be accepted by all banks and businesses, we could start anew in an instant. We could even write off all mortgages and nationalize all real estate, and have a system whereby we pay rent to the state. These kind of scenarios are hard to comprehend, but when the need is highest, solutions can become very creative.

We do not live in a binary black and white world. Rather, reality is in 256 shades of grey. It is therefore much more logical to expect an outcome for our reset to range somewhere between 1 and 256. Some debts will be cancelled. Some parts of the financial system will be nationalized, as we have seen happening with banks and other financial institutions since 2008.

A new reset will simply bring our monetary system to the next phase. All parties involved (the US, the EU, the BRICS countries, Japan, the Middle East) have so much to lose if they wait too long implementing the necessary changes. And the US knows they have the most to lose. They understand they will need to take the initiative again, just as they did in 1944 (Bretton Woods 1.0) and 1971 (Bretton Woods 2.0). The wait is on for Bretton Woods 3.0.

81. When did experts begin to understand the system had to change?

Soon after the start of the crisis in late 2008, the IMF and others began brainstorming about a next phase for our financial system. According to IMF historian James Boughton, some world leaders have been calling for a 'new Bretton woods' ever since:[276]

> What Sarkozy and Brown envisaged was a new multilateral agreement to stabilize international finance in the 21st century, the way the 1944 conference, which established the International Monetary Fund and the World Bank, stabilized financial relations among countries in the second half of the 20th century. On several occasions throughout the 20th century, political leaders in major countries sought international agreements on the global economic or financial architecture. Many of those efforts failed, Bretton Woods being the major exception.

He also gave a few examples of other proposed resets:

> 1918/19 – to redraw political borders and to establish principles for avoiding a repeat of the war, establishing a framework for restoring free trade and the flow of capital was also on the agenda.
>
> 1933 – the World Monetary and Economic Conference to re-establish fixed parities for a wider range of currencies, failed because of a lack of support from the US government. It was preceded by [the] Genoa meeting (1922) that re-established the gold standard for a group of mostly European countries, and the Rome meeting (1930) that established the Bank for International Settlements.

276 https://www.imf.org/external/pubs/ft/fandd/2009/03/boughton.htm.

In 2012, the former Bank of England Governor Mervyn King predicted advanced economies would probably not be able to get out of the current crisis without large debt restructurings and a recapitalization of the financial system (i.e. banks):

> I am not sure that advanced economies in general will find it easy to get out of their current predicament without creditors acknowledging further likely losses, a significant writing down of asset values and recapitalization of their financial systems. [...] Only then will it be possible to return to a more normal provision of the vital banking services so crucial to an economic recovery.[277]

The United Nations[278] called for 'a new Global Reserve System' based on the IMF's Special Drawing Rights (SDRs) as early as 2009.[279] The SDRs, which have been in existence since 1969, often called IMF money, were 'designed' as a medium of exchange for international transactions in case the dollar got into serious trouble. The UN report stated:

> The global imbalances which played an important role in this crisis can only be addressed if there is a better way of dealing with international economic risks facing countries than the current system of accumulating international reserves. Indeed, the magnitude of this crisis and the inadequacy of

277 http://www.bloomberg.com/news/2012-10-23/king-says-boe-stands-ready-to-add-stimulus-should-recovery-fade.html.

278 Experts of the President of the General Assembly on reforms of the international monetary and financial system, http://www.un.org/ga/president/63/letters/recommendationExperts200309.pdf.

279 The SDR is not a currency, but holders of SDRs can obtain currencies of IMF members in exchange for their SDRs. So when more SDRs are created, more money is created. It is used to allow countries to participate in foreign trade without affecting their exchange rates. The IMF can allocate SDRs to all its members in proportion to certain quotas. In 2009, the IMF increased general SDR allocation to US$250 billion, with low-income countries only 'receiving' over $18 billion. The total amount of outstanding SDRs was just over 400 billion in the summer of 2015.

> international responses may motivate even further accumulations. Inappropriate responses by some international economic institutions in previous economic crises have contributed to the problem, making reforms of the kind described here all the more essential. To resolve this problem a new Global Reserve System, what may be viewed as a greatly expanded SDR, with regular or cyclically adjusted emissions calibrated to the size of reserve accumulations – could contribute to global stability, economic strength, and global equity. Currently, poor countries are lending to the rich reserve countries at low interest rates. The dangers of a single-country reserve system have long been recognized, as the accumulation of debt undermines confidence and stability. But a two (or three) country reserve system, to which the world seems to be moving, may be equally unstable. The new Global Reserve System is feasible, non-inflationary, and could be easily implemented, including in ways which mitigate the difficulties caused by asymmetric adjustment between surplus and deficit countries.

In that same year, Governor Xiaochuan of the People's Bank of China (China's central bank) published a long statement in support of these ideas. In the statement, initially only published on the PBoC's website, he called for replacing the dollar as the dominant world currency. He also said the financial crisis showed the need for 'an international reserve currency that is disconnected from individual nations and is able to remain stable in the long run.' He also explained that the interests of the US and those of other countries should be 'aligned', which is not the case in the current dollar system. Because this statement can be seen as the start of the Chinese path toward a monetary reset the statement is published here in full:[280]

280 http://www.pbc.gov.cn/publish/english/956/2009/20091229104425550619706/20091229104425550619706_.html

The outbreak of the current crisis and its spillover in the world have confronted us with a long-existing but still unanswered question, what kind of international reserve currency do we need to secure global financial stability and facilitate world economic growth, which was one of the purposes for establishing the IMF? There were various institutional arrangements in an attempt to find a solution, including the Silver Standard, the Gold Standard, the Gold Exchange Standard and the Bretton Woods system. The above question, however, as the ongoing financial crisis demonstrates, is far from being solved, and has become even more severe due to the inherent weaknesses of the current international monetary system.

Theoretically, an international reserve currency should first be anchored to a stable benchmark and issued according to a clear set of rules, therefore to ensure orderly supply; second, its supply should be flexible enough to allow timely adjustment according to the changing demand; third, such adjustments should be disconnected from economic conditions and sovereign interests of any single country. The acceptance of credit-based national currencies as major international reserve currencies, as is the case in the current system, is a rare special case in history. The crisis again calls for creative reform of the existing international monetary system toward an international reserve currency with a stable value, rule-based issuance and manageable supply, so as to achieve the objective of safeguarding global economic and financial stability. […] When a national currency is used in pricing primary commodities, trade settlements and is adopted as a reserve currency globally, efforts of the monetary authority issuing such a currency to address its economic imbalances by adjusting exchange rate would be made in vain, as its currency serves as a benchmark for many other currencies. While benefiting from a widely accepted reserve currency, the globalization also suffers from the flaws of such a system.

The frequency and increasing intensity of financial crises following the collapse of the Bretton Woods system suggests the costs of such a system to the world may have exceeded its benefits. The price is becoming increasingly higher, not only for the users, but also for the issuers of the reserve currencies. Although crisis may not necessarily be an intended result of the issuing authorities, it is an inevitable outcome of the institutional flaws.

II. The desirable goal of reforming the international monetary system, therefore, is to create an international reserve currency that is disconnected from individual nations and is able to remain stable in the long run, thus removing the inherent deficiencies caused by using credit-based national currencies.

- Though the super-sovereign reserve currency has long since been proposed, yet no substantive progress has been achieved to date. Back in the 1940s, Keynes had already proposed to introduce an international currency unit named 'Bancor', based on the value of 30 representative commodities. Unfortunately, the proposal was not accepted. The collapse of the Bretton Woods system, which was based on the White approach, indicates that the Keynesian approach may have been more farsighted. The IMF also created the SDR in 1969, when the defects of the Bretton Woods system initially emerged, to mitigate the inherent risks sovereign reserve currencies caused. Yet, the role of the SDR has not been put into full play due to limitations on its allocation and the scope of its uses. However, it serves as the light in the tunnel for the reform of the international monetary system.
- A super-sovereign reserve currency not only eliminates the inherent risks of credit-based sovereign currency, but also makes it possible to manage global liquidity. A super-sovereign reserve currency managed by a global institution could be used to both create and control the global liquidity.

And when a country's currency is no longer used as the yardstick for global trade and as the benchmark for other currencies, the exchange rate policy of the country would be far more effective in adjusting economic imbalances. This will significantly reduce the risks of a future crisis and enhance crisis management capability.

III. The reform should be guided by a grand vision and begin with specific deliverables. It should be a gradual process that yields win-win results for all.

– The reestablishment of a new and widely accepted reserve currency with a stable valuation benchmark may take a long time. The creation of an international currency unit, based on the Keynesian proposal, is a bold initiative that requires extraordinary political vision and courage. In the short run, the international community, particularly the IMF, should at least recognize and face up to the risks resulting from the existing system, conduct regular monitoring and assessment and issue timely early warnings.
– Special consideration should be given to giving the SDR a greater role. The SDR has the features and potential to act as a super-sovereign reserve currency. Moreover, an increase in SDR allocation would help the Fund address its resources problem and the difficulties in the voice and representation reform. Therefore, efforts should be made to push forward a SDR allocation. This will require political cooperation among member countries. Specifically, the Fourth Amendment to the Articles of Agreement and relevant resolution on SDR allocation proposed in 1997 should be approved as soon as possible so that members joined the Fund after 1981 could also share the benefits of the SDR. On the basis of this, considerations could be given to further increase SDR allocation.
– The scope of using the SDR should be broadened, so as to enable it to fully satisfy the member countries' demand for a reserve currency.

- Set up a settlement system between the SDR and other currencies. Therefore, the SDR, which is now only used between governments and international institutions, could become a widely accepted means of payment in international trade and financial transactions.
- Actively promote the use of the SDR in international trade, commodities pricing, investment and corporate book-keeping. This will help enhance the role of the SDR, and will effectively reduce the fluctuation of prices of assets denominated in national currencies and related risks.
- Create financial assets denominated in the SDR to increase its appeal. The introduction of SDR-denominated securities, which is being studied by the IMF, will be a good start.
- Further improve the valuation and allocation of the SDR. The basket of currencies forming the basis for SDR valuation should be expanded to include currencies of all major economies, and the GDP may also be included as a weight. The allocation of the SDR can be shifted from a purely calculation-based system to a system backed by real assets, such as a reserve pool, to further boost market confidence in its value.

IV. Entrusting part of the member countries' reserve to the centralized management of the IMF will not only enhance the international community's ability to address the crisis and maintain the stability of the international monetary and financial system, but also significantly strengthen the role of the SDR.

- Compared with separate management of reserves by individual countries, the centralized management of part of the global reserve by a trustworthy international institution with a reasonable return to encourage participation will be more effective in deterring speculation and stabilizing financial markets. The participating countries can also save some reserve for domestic development and economic growth. With its universal membership, its unique mandate of maintaining monetary and financial stability, and as an international 'supervisor' on the macroeconomic policies of its member countries, the IMF, equipped with its expertise, is endowed with a natural advantage to act as the manager of its member countries' reserves.

– The centralized management of its member countries' reserves by the Fund will be an effective measure to promote a greater role of the SDR as a reserve currency. To achieve this, the IMF can set up an open-ended SDR-denominated fund based on the market practice, allowing subscription and redemption in the existing reserve currencies by various investors as desired. This arrangement will not only promote the development of SDR-denominated assets, but will also partially allow management of the liquidity in the form of the existing reserve currencies. It can even lay a foundation for increasing SDR allocation to gradually replace existing reserve currencies with the SDR.

This statement delivered a very strong message to the world: China is dissatisfied with the current international monetary system and eager to change the situation of its over-reliance on the US dollar. The renminbi is unlikely to challenge the dollar any time soon and its pivotal position in world money for many years, but it probably will become number two currency before 2025.

82. What were the reactions to Zhou Xiaochuan's statement?

After the publication of the article by Zhou Xiaochuan, in which he said that it was regrettable that John Maynard Keynes' 'farsighted' Bancor proposal was not adopted at the Bretton Woods conference in 1944, China Security published an article entitled: 'Debating the International Currency System: What's in a Speech?'[281], written by two Chinese insiders on international relations. It was a study of Zhou's speech and quoted several Chinese reactions to his proposal.

The President of the China Export-Import Bank and former PBoC Vice Governor, Li Ruogu, explained:

> It shows clearly how unreasonable the current international monetary system is. […] it may be feasible to reform the existing SDR into a payment currency in a real sense and further to substitute the dollar-denominated currency by a basket of currencies commonly accepted by all countries. To be more specific, a new Bretton Woods System focusing on a basket of currencies should be established […] The medium-term goal of the Chinese proposal is about reforming the International Currency System, in which a core component is rethinking the selection of standard currency for international reserves.

The report concluded with a spot on analysis about the crisis' effects on the dollar system:

> Chinese observers have noted that the current crisis could well turn out to be a watershed event in the primacy of the dollar and the life of the dollar system […] The consensus Chinese view is that a multi-reserve currency era is coming, even if only gradually, and that it would be in China's strategic

281 http://www.isn.ethz.ch/Digital-Library/Publications/Detail/?lang=en&id=117049.

interests to promote such a scenario [...] One vision of such a multi-polar, decentralized and diversified currency system that has been offered by Chinese analysts is the dollar, the euro and a 'regional Asian currency [renminbi? – WM]' sharing the role of global reserve currency – and together backstopped by SDRs.[282]

In China, a few more studies for changes to the current monetary system have been published as well.[283] There are also some very strong statements in 'The road map of the reform of the international monetary and financial system' (2009), which can be found at the website of the United Nations.[284]

The author Yu Yongding, a former member of the Monetary Affairs Committee of China's central bank and one of the country's most influential economists, suggests that the inherent flaws in the dollar system are easy to miss because of the importance of dollar assets in the investment portfolio of international investors. This has meant that foreign exchange funds have flowed back into the United States. The report, published by the prestigious Institute of World Economics and Politics (IWEP), part of the Chinese Academy of Social Sciences, in early 2009, shows very clear what the Chinese elite really thinks about the current dollar/IMF-centred system. According to the author, 'the lack of independence has damaged the authority of the IMF irretrievably. Any reform of the IMF less than a total overhaul is not acceptable.' This report is also very important for understanding the Chinese position:

282 When US Secretary of the Treasury Timothy Geithner was asked about Governor Zhou's call for international currency reforms in 2009, he said that while he had not read the proposal he anticipated that the plan was 'designed to increase the use of the IMF's special drawing rights. And we're actually quite open to that.'

283 http://en.iwep.org.cn/upload/2013/02/d20130217144133297.pdf.

284 Some Thoughts on Current International Financial Crisis and East Asia's Responses Yu Yongding, IWEP, CASS, 20 January 2009.

The global financial and economic crisis has reached a critical stage [...] When helicopter-Ben drops tons and tons of dollar bills from the sky, what value does the dollar still have? When the balance sheet of the Fed is no better than a junk bond fund, it becomes a kind of junk bond fund. The Fed knows very well the inflationary consequences of the extremely loose monetary policy. Hence it has brought forward some new schemes, such as paying interest on reserves and possible selling Fed bonds to the financial institutions. However, the basic question is still unanswered: when the situation has changed, can the Fed withdraw the liquidity quickly enough to prevent current liquidity shortage and credit crunch from turning into hyper-inflation and a free fall of the US dollar? In other words, will the US inflate away its debt burden? The result of such an inflation and devaluation scenario, let alone defaults, will be devastating for China, Japan and the rest of the East Asian countries, which hold some 3 trillion USD foreign exchange reserves, collectively. Currently, the Chinese government is facing two major challenges: minimizing the negative impact of the US financial crisis-led global slowdown on economic growth, and preserving the value of its foreign exchange reserves, which mostly are in the form of the US treasuries. More or less, this is an issue common to all North Asia. Hence the discussion of the reform of international financial system should put the issue of preserving the value of foreign exchange reserves high on the agenda. No matter what policies the US government has adopted and will adopt, the stabilization of US financial market and US economy should not be achieved at the expense of the rest of the world. No matter whether it is a devious attempt or unintended result, if serious inflation and a dramatic fall of the US dollar are allowed to happen, the consequences will be extremely grave. In other words, US policy in dealing with current financial crisis is not a pure sovereign matter but that it is an international matter [...] There should be a new framework to facilitate policy coordination among all major sovereign stakeholders in the world.

In the long run, the key issue is that the US dollar's hegemonic position, as virtually the sole international reserve currency should be changed. Because America's liabilities are denominated in terms of dollars, held by foreign countries as American assets, there are no effective disciplines can be imposed on the US monetary authority, and the smooth functioning of other sovereign countries will dependant entirely on the good-will and competency of the US monetary authority. The current US financial crisis has damaged the credibility of US authorities and the dollars permanently, and shown that to use the dollar as the only store of value, unite of account, and vehicle money is an unaffordable luxury for the rest of the world [...] We do not know what will be the next step or misstep of the Fed and the Ministry of Treasury will take, let alone the possible consequences. China, as the biggest holder of the US Treasuries, is asking the question as Rogoff did: 'Why would a government refuse to pay its domestic public debt in full when it can simply inflate the problem away?' The Chinese government has demanded guarantees by the US government for the safety of China's assets in the US. I do not know whether the Chinese government has got such any guarantees, or whether the US government has the ability to keep the promise, if they were given. No matter whatever the result is, the long-term solution lies in the reform of the international financial system that is characterized by the fact that the US dollar is the major reserve currency. The issue of a new reserve currency, a basket of reserve currencies or whatever, which will not be subject to the influence of a major country's domestic policy, should be high on the agenda of the reform of international financial system. Otherwise, the discussion of the reform of the international financial system cannot be very meaningful.

From China's perspective, there are three basic roads for the reform of the international monetary system: reform within the current framework of international monetary system, strengthening regional financial cooperation and integration, and the internationalization of the RMB.

The reform of post Breton Woods system from within. The reform within the current framework means the reform of the IMF. Since the Asian Financial Crisis, the IMF's authority and credibility have deteriorated rapidly by its own missteps. Before 2007, the IMF failed to do anything to supervise, regulate, and contain the huge asset bubbles in international capital market. It even failed to forewarn the world on the coming subprime crisis in any significant way, let alone to had done anything to prevent the crisis from forming and breaking out since the turn of the century. Has IMF ever exposed the excess of the US financial institutions? Has the IMF ever pointed out that MBS, CDO and CDS have dangerous implications to the financial stability? Now has the IMF ever raised any questions on the Fed's desperate monetary policy? In 2008, the most important decision taken by the IMF was to toe the line of the US government to designate China as exchange rate manipulator. Here there is no need to discuss whether China erred or not. The thing is that the IMF has lost the sense of direction. I do not doubt the intellectual competency of IMF staffers. The thing is political influence. Lack of independence has damaged the authority of the IMF irretrievably. Any reform of the IMF less than a total overhaul is not acceptable. As a first step, voting share should be redistributed, and the role of East Asian countries should be increased significantly.

To make the IMF a more balanced international organization. The influence of the US should be reduced. Asia must have bigger say in the organization. At the operational level, there are five major issues should be discussed.

– First, the SDR should play a more important role. The question of whether and how the SDR should replace the US dollar as a reserve currency should be considered seriously.

– Second, how the BIS and the IMF should strengthen their cooperation so as to improve the supervision of financial stability in the global financial market.
– Third, IMF conditionality should be totally reconsidered. The action taken by the US government in dealing with current financial crisis has totally discredited the prescriptions provided to and imposed on the crisis-affected countries during the Asian Financial Crisis.
– Fourth, now we have G7-8, G20 and G whatever. How the division of labour of these forums and the IMF should be defined more clearly. Maybe, the UN should have more say on international finance and the IMF should be more cooperative with the UN.
– Last but not least, the IMF has been pushing capital account liberalization dogmatically. It should play a more positive role in helping developing countries in strengthening the management of Cross-Border Capital Flows. So far, the impact of the US financial crisis on Korea seems gravest in East Asia. I am wondering whether this is attributable to the unhindered cross-border capital flows. Korea allowed too much capital aimed at arbitrage and speculation to inundate its financial market after having implemented faithfully the IMF prescriptions during the Asian financial crisis. Now the Korea seems have no effective means to prevent capital from flowing out, which is attributable to the unwinding of carry-trade, and withdrawing of foreign capital because of liquidity shortage, credit crunch and need for capital injections. The IMF should adjust its position on capital account liberalization. The blindly push of free flows of cross-border capital flows should be stopped and a more measured attitude should be adopted by the IMF.

On regional financial cooperation:
– The dissatisfaction felt by Asian countries to the IMF's insensitivity toward Asian countries' suffering found its

initial expression in Japan's proposal of establishing an Asian Monetary Fund (AMF).

– On the whole, during the current global financial crisis, the performance of the East Asian governments in terms of financial cooperation and coordination is rather disappointing [...] Why can the 13 countries not get together and take concerted acts to demand the US government to safeguard the safety of their hard-earned foreign exchange reserves, which are mostly in the form of the US government securities. Are the governments in the region so sure that their people's assets are safe and the US government will not get rid of its huge debt burden by inflation, devaluation of the US dollar and defaults?

83. Why is a monetary reset desired by China?

In recent years, the Chinese calls to get rid of the so-called 'dollar trap' have intensified.[285] In 2011, the Chinese newspaper *People's Daily* criticized the irresponsibility of the US debt policy. Two years later, in 2013, the state news agency Xinhua distributed a commentary declaring that the time had come to 'de-Americanize' the world. What is remarkable about this article from our perspective is that it, in effect, calls for a Big Reset of the system and even the need for a 'new global financial system' that is not dependent on the US. Given the importance of the article, I quote from it extensively here:[286]

> As US politicians of both political parties are still shuffling back and forth between the White House and the Capitol Hill without striking a deal to bring normality to the body politic they brag about, it is perhaps a good time for befuddled the world to start considering building a de-Americanized world [...] instead of honoring its duties as a responsible leading power, a self-serving Washington has abused its superpower status and introduced even more chaos into the world by shifting financial risks overseas, instigating regional tensions amid territorial disputes, and fighting unwarranted wars under the cover of outright lies.
>
> As a result, the world is still crawling its way out of an economic disaster thanks to the voracious Wall Street elites, while bombings and killings have become virtually daily routines in Iraq, years after Washington claimed it has liberated its people from tyrannical rule.
>
> Most recently, the cyclical stagnation in Washington for a viable solution on a bipartisan federal budget and an approval for raising debt ceiling has again left many nations' agonized

285 In 2013, over 30% of China's foreign financial reserves was held in the form of US dollar assets.

286 http://news.xinhuanet.com/english/indepth/2013-10/13/c_132794246.htm.

> tremendous dollar assets in jeopardy and the international community highly agonized.
>
> Such alarming days when the destinies of others are in the hands of a hypocritical nation have to be terminated, and a new world order shouldering be put in place, according to which all nations, big or small, poor or rich, can have their key interests respected and protected interests on an equal footing.
>
> To that end, several cornerstones shouldering be laid to underpin a de-Americanized world […] the world's financial system has to embrace some useful substantial reforms.
>
> The developing and emerging market economies need to have more say in major international financial institutions including the World Bank and the International Monetary Fund, so that they could better reflect the transformations of the global economic and political landscape.
>
> What may also be included as a key part of an effective reform is the introduction of a new international reserve currency that's to be created to replace the dominant US dollars, so that the international community could permanently stay away from the spillover of the Intensifying domestic political turmoil in the United States.
>
> Of course, the purpose of its promoting changes thesis is not to completely toss aside the United States, Which is useful impossible. Rather, it is encouragement to Washington to play a much more constructive role in addressing global affairs.
>
> And among all options, it is suggested that the beltway politicians first start with ending the pernicious impasse.

Chinese officials frequently point out that diversifying too rapidly out of the dollar would risk triggering a precipitous decline in the US currency, which would in turn erode the value of China's significant dollar holdings. Similar considerations apply to the euro: if the Chinese were to sell a significant amount of its euros during a period of euro weakness, this would depreciate the value of one of its core currency holdings.

Whatever doubts and possible setbacks the Chinese may have had with regard to the world's two main reserve currencies, they have no other currency options given the size of China's foreign exchange reserves. This is likely to have been an important reason why the Chinese authorities have decided in recent years to boost the share of gold in their country's reserves.

84. Will gold be part of a currency reset?

While most experts believe there will be no return to a full gold standard, gold will probably play a much greater role in the next phase of the financial systems.

The aforementioned OMFIF report points toward the likelihood of gold growing in importance within the international financial system:

> The role of gold during and after a move to a multi-currency reserve system is an important issue. Gold will probably play a greater role during the transition period. This is likely to be a period of substantial fluctuation in currency values as market actors attempt to find a new equilibrium. That is where the attraction of gold, an asset that is nobody's liability should stand out [...] Any sizeable increase in distrust of politicians, founded on suspicion that they – or central bankers – are debasing the currency, is likely to increase the attraction of gold as a hedge against all currencies [...] As the international community attempts to take on these challenges, gold waits in the wings. For the first time in many years, gold stands well prepared to move once more toward the center-stage. This could be the start of an immensely important phase in the history of world money.

The OMFIF has also called for extending a new SDR to include the so-called R-currencies – the renminbi, rupee, real, rand and ruble – and possibly gold:

> By moving counter-cyclically to the dollar, gold could improve the stabilizing properties of the SDR. Particularly if the threats to the dollar and the euro worsen, a large SDR issue improved by some gold content and the R-currencies may be urgently required [...] So well before the renminbi advances to a reserve currency status, gold might return to the heart of the system.

If we have learned anything from the history of money, it is that gold (or silver) have always been needed to rebuild trust in monetary systems. The former president of the Dutch central bank, Jelle Zijlstra, wrote in his biography:

> The intrinsic value of gold along with its romantic image has until the 1960s dominated the international monetary framework. It was perhaps a rather irrational anchor, however it was a stable anchor. Eventually, this changed, not because old-fashioned understandings had been replaced by more modern ones, but because the United States of America found the role of the dollar threatened by gold.

But now, some forty years later, the US may consider it useful to bring back gold to support the dollar.

Some American insiders have even been calling openly for a return to the gold standard. One such insider is neo-conservative Robert Zoellick, the former President of the World Bank, who wrote an open letter to the Financial Times in 2010 entitled 'Bring back the gold standard':

> The G20 should complement this growth recovery programme with a plan to build a co-operative monetary system that reflects emerging economic conditions. This new system is likely to need to involve the dollar, the euro, the yen, the pound and a renminbi that moves toward internationalization and then an open capital account. The system should also consider employing gold as an international reference point of market expectations about inflation, deflation and future currency values. Although textbooks may view gold as the old money, markets are using gold as an alternative monetary asset today [...] The development of a monetary system to succeed 'Bretton Woods II', launched in 1971, will take time. But we need to begin. The scope of the changes since 1971 certainly matches those between 1945 and 1971 that prompted the shift from Bretton Woods I to II.

According to Steve Forbes,[287] CEO of the eponymous magazine and an advisor to some of the 2012 presidential candidates, the 'debate should be focused on what the best gold system is, not on whether we need to go back to one.' It was therefore no surprise to see an interview with Professor Robert Mundell in Forbes Magazine in which he argues for a return to the gold standard for both the dollar and the euro.[288]

Mundell is seen as one of the architects of the euro and has been an advisor to the Chinese government. Mundell remarked:

> There could be a kind of Bretton Woods type of gold standard where the price of gold was fixed for central banks and they could use gold as an asset to trade within central banks. The great advantage of that was that gold is nobody's liability and it can't be printed. So it has a strength and confidence that people trust. So if you had not just the United States but the United States and the euro (area) tied together to each other and to gold, gold might be the intermediary and then with the other important currencies like the yen and Chinese Yuan and British pound all tied together as a kind of new SDR that could be one way the world could move forward on a better monetary system.[289]

287 http://www.forbes.com/forbes/2011/0606/opinions-steve-forbes-fact-comment-gop-prez-wannabes.html.
288 Mundell endorsed the gold standard on Pimm Fox's Bloomberg Television 'Taking Stock'.
289 http://www.forbes.com/sites/ralphbenko/2011/06/13/the-emerging-new-monetarism-gold-convertibility-to-save-the-euro.

85. Will China choose the path of cooperation or confrontation?

Since 2010, the Chinese banker Min Zhu has been the highest ranking Chinese banker within the IMF. He started as a special advisor in 2010 and was promoted to one of the four deputy managing directors directly under the IMF's managing director, Christine Lagarde. Zhu is the third Chinese to take on a senior position in an international financial institution. Shengman Zhang was a Managing Director of The World Bank and Justin Yifu Lin a former vice president and chief economist of The World Bank.

Since the Bretton Woods conference in 1944 a gentleman's agreement has been in effect that means the IMF's managing director is always a European and the president of the World Bank always an American. This 'agreement' is increasingly being questioned and many expect these two posts may soon open up to a candidate from one of the BRIC countries. (Brazil, Russia, India or China).

During the start of the roadshow for the internationalization of the renminbi in London in 2014, Professor Zhenya Liu remarked, 'China has a big population, and it needs a big chair in the (IMF) room.' According to the Chinese, the governance of the IMF needs to better represent the growing significance of developing economies. 'Excluding 20% of the world's population isn't good for anyone,' he said.

In an op-ed in the New York Times, titled 'The IMF needs a reset', two Western scholars explained that the IMF is experiencing a crisis of governance because:

> the governments of big developing countries become frustrated with the unwillingness of Western countries to adjust the distribution of power in the fund in line with their rising economic weight.

They point to the fact the four big BRICS have a combined share of almost 25% of world GDP, compared to just over 13%

for the four big European economies (Germany, France, Britain, Italy). But the four BRIC countries have only 10% of the IMF votes, compared with almost 18% for the four European nations. While China has been financing the US for over one trillion dollars since 2000, they have less than 4% of the IMF votes, compared to 16% for the US.[290] Of course, the US is doing everything possible to postpone the needed changes.

The growing divisions between the East and the West also came to light when OMFIF published a list of the main issues of the global economy after touring Asia in the summer of 2014:

> – Policy divisions between Western and Asian economies seem to be growing. Increased Asian confidence and resilience are accompanied by belief that the West (and especially Europe) has lost its way. One Asian sovereign fund leader contrasted Asia's emphasis on long term returns with the short-termism and greed of Western investors. 'The result of the global financial crisis was that the man in the street was devastated while bankers enjoyed their bonuses.' He highlighted the difference between Western rigour on Asia over the 1997-98 financial crisis and European compromises made toward indebted countries in the EMU crisis.
>
> – There is considerable suspicion about the IMF and an excessively Washington-focused view of the world. Quota reforms and governance changes at Bretton Woods institutions remain stymied by congressional refusal to ratify them. The result is frustration in leading Asian countries and a number of moves – whether through the Chiang Mai reserves-pooling initiative or the latest plan for a BRICS bank – for emerging markets to lower their IMF dependence.
>
> – Internationalization of the renminbi is proceeding on many fronts. The Chinese authorities now accept that the

290 http://en.wikipedia.org/wiki/International_Monetary_Fund.

> renminbi is, de facto, part of a multiple reserve currency system in which the dollar continues to play the leading role.

But China has made clear they would prefer to choose the path of cooperation instead of confrontation although they would prefer to start with a ‘new world central bank’.

86. Are there any Western studies on a monetary reset?

In a Chatham House study titled 'Beyond the Dollar Rethinking the International Monetary System' (2010),[291] the question for a needed reform of the current monetary system was studied by experts from the West and East as well.[292] It also called for an 'expansion of the role of the IMF's Special Drawing Rights'.

The report recommended the following changes to the international monetary system:

– Develop a multicurrency reserve system that is appropriate for a world of regional trading blocs – Europe, Asia, the Americas – alongside a still preeminent dollar.

– Encourage a more extensive use of Special Drawing Rights as a supranational currency alongside international reserve currencies that are issued by sovereign states or by sovereign states pooled together in a currency union, as is the case for the euro. Take steps to increase the use of and demand for SDRs, beyond official circles, in international trade and finance. The IMF should permit SDR accounts to be opened by private sector actors.

The Chinese, who participated in this study called for another study because they were surprised that a possible new role for gold was not mentioned.[293]

291 http://www.chathamhouse.org/publications/papers/view/109263.
292 http://www.worldeconomyandfinance.org/PDFs/beyond_the_dollar.pdf.
293 From the report: 'On behalf of Chatham House, I thank all those organizations that in different ways supported the work of the Taskforce, in particular the Chinese Academy of Social Sciences (CASS), and Professor Yu Yongding and Mr Zhang Yuyan. We hope that this report does justice to the confidence they placed in us.' http://www.chathamhouse.org/sites/files/chathamhouse/public/Research/International%20Economics/r0212gold.pdf.

This led to a new study by the Chatham House Gold Taskforce titled 'Gold and the International Monetary System', which was published early 2012. The group acknowledged that gold bullion could serve as a hedge against the declining values of fiat currencies and that it plays a role as a reserve asset, but concludes that for the bullion to play a more formal role in the international monetary system, 'it would be imperative that it neither hinders the system's performance nor creates unacceptable constraints on national economic policies.'

The report even mentioned the idea that gold could be added to the SDR's currency basket:

> – Although an intriguing idea was considered by the Taskforce – to expand the IMF's SDRs basket to include gold – the proposal failed to convince most members of the group that this would actually bolster the international monetary system. In future, adding currencies from key developing countries, such as China, was thought to be desirable by many Taskforce members to better reflect their growing importance in the world economy.

One of the members of this Taskforce was House of Lords representative Lord Meghnad Desai,[294] who published a note around the same time in which he mentioned a role for gold within the SDR again:

> There are several ideas about gold – as a monetary base on its own, as an addition to the SDRs to 'harden them, as a 'circuit breaker' which gives an early warning as to the impending dangers.

In 2015, he sounded even more convinced about a future gold-backed SDR at a precious metals conference in Dubai:

294 Lord Desai is also chairman of the London based monetary think tank OMFIF.

We could ask that gold be nominated as part of the SDR. That is one thing I think is quite likely to happen. This will be easier if China increases its official gold holdings.[295]

295 http://www.zerohedge.com/news/2015-04-12/gold-backed-sdr-quite-likely-happen-lses-lord-desai-warns.

87. So this explains why China has been all over gold since 2010?

The fact that China and other Asian countries (including Russia) are buying massive amounts of gold shows they think gold will play a larger role in the future phase of the monetary system. In the last few years we have seen a large move of physical gold from West to East. Huge Indian gold imports led to a huge distortion of India's trade balance, a collapse of the rupee (2013) and even an extra 10% import duty on gold. Russia has tripled it gold reserves since the start of the credit crisis in 2007. While Western banks are trying to scare customers away from buying gold China has been promoting precious metals as safe havens. Over 100,000 retail outlets sell gold and silver to the general public. A detailed analysis of the Chinese gold market shows almost 9,000 tonnes of physical gold have left the vaults of the Shanghai Gold Exchange (SGE) since 2009.

This does not include any gold buying for official Chinese central bank holdings, which are considered to be a state secret. In 2009, the PBoC published a doubling of its gold holdings after years of silence and in July 2015 the PBoC updated the gold reserves again, from 1054 to 1658 tonnes. In an online statement the Chinese central bank acknowledged it is accumulating much more gold in a program named 'Hiding gold with the people'. Gold bought by ordinary Chinese can always be confiscated in times of crisis:[296]

> Gold at a particular time is a good investment. But the capacity of the gold market is small compared with the scale of China's foreign exchange reserves. If a large number of foreign exchange reserves would (be used) to buy gold, this could easily lead to impact on the market … 'hiding gold with the people', has been the current situation.

296 http://www.pbc.gov.cn/publish/goutongjiaoliu/524/2015/20150717164205743449367/20150717164205743449367_.html.

China currently holds some 1.5% of its foreign exchange reserves in gold, which is relatively low compared with developed countries and some developing countries. China would like to grow that percentage toward at least 5-10%, which would translate into roughly 5,000-8,000 tonnes, according to Song Xin, Party Secretary and President of the China Gold Association. In 2014 he wrote an article ‘Gold will Support Renminbi as it Moves to Join World’.[297]

> For China, the strategic mission of gold lies in the support of renminbi (RMB) internationalization, and so let China become a world economic power and make sure that the ‘China Dream’ is realized. Gold is the only thing carrying the dual mantels of a commodity as well as a monetary substance. It’s both a very ‘honest’ asset and forms the very material basis for modern fiat currencies. Historically, gold has played an irreplaceable role in responses to financial crises and wars as it comes to protecting a country’s economic security. Because of this, gold carries with it an honored and divine-given strategic mission in the ascent of the Chinese people and the pursuit of the ‘China Dream’.
>
> Gold is the world’s only monetary asset that has no counterparty risk, and is the only cross-nation, cross-language, cross-ethnicity, cross-religion and cross-culture globally recognized monetary asset. Gold is the last protection for a country’s economic security; it safeguards a nation’s sovereignty in times of crises. A textbook example happened in 1997 during the Asian financial crisis. To work through Korea’s severe debt problem, the IMF’s condition for a rescue package was to sell large enterprises. In the end, the Korean government had no choice but to call on its people to donate gold to settle the foreign debt, and it was only through this act that the chaebols at the center of the country’s economy and independence survived.

297 http://finance.sina.com.cn/nmetal/tzzs/20140730/153019863945.shtml.

From our country's point of view, gold has played an irreplaceable role in the development of our economic society. In the wars during the Revolution [1921-1937] gold provided strong support in the economic development of the liberated zones and achievements in reforms; in the three years of natural disasters, the nation used gold reserves to obtain information on living and production conditions and took actions to alleviate hardship. At the start of the great Reforms (1980s), gold boosted our foreign reserve levels and helped the promising private sector and it advanced society. After 1989, we suffered economic sanctions from Western countries for a while and the PBoC used our gold reserves to enter into swap agreements to obtain needed foreign currencies. Right now, gold is still serving its functions to protect against economic risks; contributing in ever more important ways to our financial security. For the moment, although in general the international scene is peaceful, conflicts can develop in certain regions. If there should be a blockade or regional war, there could be only one method of payment left: gold.

Gold is a monetary asset that transcends national sovereignty, is very powerful to settle obligations when everything else fails; hence it's exactly the basis of a currency moving up in the international arena. When the British Pound and the USD became international currencies, their gold reserve as a share of total world gold reserves was 50% and 60% respectively; when the Euro was introduced, the combined gold reserves of the member countries was more than 10,000 tonnes, more than the US had. If the RMB wants to achieve international status, it must have popular acceptance and a stable value. To this end, other than having assurance from the issuing nation, it is very important to have enough gold as the foundation, raising the 'gold content' of the RMB. Therefore, to China, the meaning and mission of gold is to support the RMB to become an internationally accepted currency and make China an economic powerhouse.

In this view, our gold reserves are very low, both in terms of a nominal level as well as a percentage of official reserves. From the nominal level, the total official reserves of gold in the world stands at 30,000 tonnes, of which the USA has been occupying the first place at 8133.5 tonnes – 26% of the world total. Germany has 3387.1 tonnes and Italy and France both hold more than 2,400 tonnes. Ours is 1054 tonnes at the sixths place – only 3.4% of the world total. As a percentage of a country's total reserves, US gold reserves amount to 71.7 % and European nations have kept their levels between 40% to 70%. The average of the world is about 10%, but for us it's only 1%.
That is why, in order for gold to fulfill its destined mission, we must raise our gold holdings a great deal, and do so with a solid plan. Step one should take us to the 4,000 tonnes mark, more than Germany and become number two in the world, next, we should increase step by step toward 8,500 tonnes, more than the US.
How to achieve growth in our gold reserve? Apart from the PBoC directly buying in the open market, we should use also use the following strategies:

1. Relax gold import controls […] By relaxing import controls, the large-scale gold companies can then obtain this gold […] and turn gold into official reserves as required.
2. Establish a gold reserve building fund. This can be seeded using capital from the State Treasury, and open it for participation by private-sector capital in the public. It should be controlled by the State and used to target diverse off-shore gold resources, acquire mines and raw gold.
3. Establish a Gold bank. We need to establish our gold bank as soon as possible, and enable it to break the barrier between the commodity and monetary world. It can further help us acquire reserves and give us more say and control in the gold market […] its business would include: gold pricing (fix), gold financing and leasing, gold-guaranteed payments, gold

> saving accounts, gold lending, gold production chain financing and issuance and trading of paper gold and other gold investments. This gold bank can then naturally use market-oriented methods to change commodity gold into monetary gold reserves, thus help us increase our strategic gold reserves.

So the Chinese understand that gold has been used time and again to rebuild faith when a fiat money system has reached its endgame.

88. Any more information about China's gold card?

In 2012, the main academic journal of the Chinese Communist Party's Central Committee published an article that sheds light on China's strategy. The article was written by Sun Zhaoxue, president of both the China National Gold Corporation (CNG) and the China Gold Association (China Gold).[298] In 2011, he received the 'economic person of the year award' during a TV show broadcast live on CCTV, the state television channel. But in 2014 he was a suspect in an anti-corruption campaign targeting 'flies', lower-placed officials, as well as high profile officials (tigers).

The essence of his article was only picked up in the West when it was translated a year later.[299] He explains how China has a strategy of hoarding gold in order to safeguard the country's economic stability and to strengthen its defense against 'external risks', which could be translated as a collapse of the dollar or the euro or even the global financial system. Even more remarkable was his view that civil hoarding of gold was just as important for the Chinese national gold strategy:

> Individual investment demand is an important component of China's gold reserve system; we should encourage individual investment demand for gold. Practice shows that gold possession by citizens is an effective supplement to national reserves and is very important to national financial security. Because gold possesses stable intrinsic value, it is both the cornerstone of countries' currency and credit as well as a global strategic reserve. Without exception, world economic powers established and implement gold strategies at the national level.

298 http://koosjansen.blogspot.nl/2013/09/building-strong-economic-and-financial.html.

299 http://koosjansen.blogspot.nl/2013/09/building-strong-economic-and-financial.html (The original version appeared on 1 August 2012 in Qiushi magazine, the main academic journal of the Chinese Communist Party's Central Committee).

So while the US and the EU try to discourage its citizens from buying gold, China wants them to buy as much gold as possible.[300]

In the same article, Zhaoxue outlines why substantial national gold reserves are so important for countries like China:

> In the global financial crisis, countries in the world political and economic game, we once again clearly see that gold reserves have an important function for financial stability and are an 'anchor' for national economic security. Increasing gold reserves should become a central pillar in our country's development strategy. International experience shows that a country requires 10% of foreign reserves in gold to ensure financial stability while achieving high economic growth concurrently. At the moment, the US, France, Italy and other countries' gold accounts for 70% of forex reserves. After the international financial crisis erupted, (our) gold reserves were increased to 1054 tons but gold reserves account for less than 1.6% of financial reserves – a wide gap compared to developed countries.

Other senior Chinese officials have also called for a substantial increase in official gold holdings in the light of the worldwide debasement of currencies. The head of the research bureau at the People's Bank of China, Zhang Jianhua, said in an interview:

> The Chinese government should not only be cautious of the imported risk caused by rising global inflation, but also further optimize its foreign-exchange portfolio and purchase gold assets when the gold price shows a favorable fluctuation. No asset is safe now. The only choice to hedge risks is to hold hard currency – gold.

300 On national television, commercials have been shown telling the Chinese how they can easily buy gold and silver. http://rare-panda-coins.blogspot.nl/2009/09/chinese-tv-promotes-gold-and-silver.html.

To increase its gold exposure, China is also investing in foreign gold producers. According to Zhaoxue, the Chinese government is intent on accumulating 'additional high quality (gold) assets':[301]

> The state will need to elevate gold to an equal strategic resource as oil and energy, from the whole industry chain to develop industry planning and resource strategies [...] increasing proven reserves, merger and acquisitions, base construction and opening up offshore gold resources to accelerate increase of national gold reserves. Concurrently, actively implement a globalization strategy that will exploit overseas resources and increase channels to grow China's gold reserves. We should achieve the highest gold reserves in the warfare time.

In a company presentation, China National Gold (CNG) explains that China has an 'aggressive acquisition strategy' of large gold deposits worldwide. Because of this, the Chinese see CNG and some other Chinese mining companies as an optimal acquisition vehicles of international targets.[302]

China has overtaken South Africa as the world's largest gold producer, and it overtook India as the world's largest gold consumer in 2013. All national gold production is added to the national reserves, but the country also imports huge amounts of gold. Since the beginning of 2013, almost as much physical gold has been leaving the vaults of the national Shanghai Gold Exchanges every month as all worldwide goldmine production combined.

301 http://www.chinagoldintl.com/corporate/mission_statement/.
302 http://www.chinagoldintl.com/investors/presentations/ (slide 7, presentation September 2013).

89. Other monetary reset scenarios: looking further into the future

In 2014, the prominent Chinese economist Justin Lin published his book,[303] *Demystifying the Chinese Economy*, in which he proposed the creation of a new international currency, which he called 'paper gold' (p-gold). National currencies could then be pegged to this new currency in the same way that they used to be pegged to gold. In an interview with the Wall Street journal he explained why:

> By 2030, we will be moving to a world of multiple reserve currencies. The US dollar, euros and Chinese yuan, are likely to be the major reserve currencies. All these three economies will be around the same size then. Many people argue that a competitive reserve currency system will be stable because competition will discipline countries. If a country doesn't act responsibly, money will flow out and it could lose its status as reserve currency country I'm doubtful this will be stable. I don't think all the major countries will be able to implement all the structural reforms necessary. As a result, there would be a lot of opportunities for speculators to point to one country, say it has structural problems and is dangerous, and bet that people will move money out of one country into another. It would be like musical chairs. Instead, we need a supranational currency. Paper gold would be a supranational currency. Each country could use it as reserve to issue its own national currency. P-gold can avoid the inherent conflict of national interest and global interest when a national currency is used as a global reserve currency. The amount of paper gold each year could be increased according to certain principles, to avoid the inherent deflationary tendency of using gold as a reserve. If you try to retain multiple reserve currencies, every country will be hurt.

303 http://www.amazon.com/Demystifying-Chinese-Economy-Justin-Yifu/dp/0521181747.

In his first book, *Currency Wars*, Jim Rickards describes a scenario in which a new gold-backed dollar could be introduced in the US:

> A 'new' gold dollar will be created at ten times the value of the old dollar. A windfall profits tax of 90% would be imposed on all private gains from the upward revaluation of gold.

According to Rickards, such a gold revaluation, including a new gold-backed dollar, is one of the last instruments available to the Fed to avoid a total collapse of the dollar system. A revaluation may be needed because the Fed is quite insolvent, with a balance sheet that has grown to almost $3,500 billion. Surprisingly, the value of all international financial reserves of the US is only around 150 billion (including $11 billion in gold reserves), slightly more than Mexico's reserves and significantly less than Algeria's ($190 billion). To put this into perspective, China has some $3,500 billion in financial reserves, while Japan has over $1,300 billion.

One of the reasons for this low number is that the US, just like the IMF, still values gold at the historical price of just $42 per ounce. This is unusual because the ECB and many other central banks value their gold reserves at market prices. Perhaps the US government hopes to spread the message that gold is a metal with little value, while the dollar is the value of choice. A revaluation of the 9,000 tonnes of US gold reserves to $8,000 per ounce would mean over $2.2 trillion in gold assets instead of $11 billion at the time of writing.

China wants to increase its gold reserves 'in the shortest time' possible to at least 8,000 tonnes. This amount would put the Chinese on a par with the US and Europe on a gold-to-GPD ratio. This would open the way for a possible joint US-EU-China gold revaluation to support the financial system when needed. Such a reset could also be backed by Russia, which has accumulated over 1,000 tonnes, most of it since the start of the credit crisis in 2007.[304]

The UK only has some 300 tonnes of gold left after selling a large portion of their reserves near the bottom in 1999 to help

304 http://goldnews.bullionvault.com/china_gold_10000_120120092.

the US hold the price of gold down.[305] A study shows that most of China's gold imports in 2013 came from London vaults. This gold was first refined in Switzerland before it moved, probably permanently, from West to East.

The Chinese realize that the US could surprise the world with a unilateral gold revaluation. Wikileaks revealed a cable, sent from the US Embassy in Beijing in early 2010 to Washington, in which a Chinese news report[306] about the consequences of such a dollar devaluation was quoted:

> If we use all of our foreign exchange reserves to buy US Treasury bonds, then when someday the US Federal Reserve suddenly announces that the original ten old US dollars are now worth only one new US dollar, and the new US dollar is pegged to the gold – we will be dumbfounded.

Gold revaluations or fiat money devaluations have been debated by many experts, as it may be the only way to prevent worldwide hyperinflation. According to Ben Davies, co-founder and CEO of Hinde Capital, revaluing gold to back up and reset the monetary system could be one of the least disruptive ways out of the credit mess.

Tocqueville Gold Fund manager John Hathaway has also discussed the prospect of a serious and sudden revaluation of gold. In an interview, he remarked that he was afraid that people might lose confidence in central banking much sooner than most people think.[307] Hathaway knows what he is talking about, since he built his fund and fortune during the gold bull market of the 1970s when another crisis of (dollar) confidence was being fought.

305 Worldwide total gold holdings (public and private) are estimated to be around 160,000 tonnes. This is close to the amount of all gold ever produced. Gold will almost always be recycled, as it is so valuable.
306 http://www.forbes.com/sites/ralphbenko/2012/10/01/signs-of-the-gold-standard-emerging-in-china/.
307 http://kingworldnews.com/kingworldnews/KWN_DailyWeb/Entries/2013/6/13_Hathaway_-_Gold_To_Shock_World_With_Rapid_$1,000_Advance.html.

90. Does China understand the US war on gold?

In recent years, there have been numerous statements clearly showing that China has a good understanding of the 'dark forces' on Wall Street.[308] PBoC governor Zhou Zhaoxue revealed in his article that the Chinese do understand the hypocrisy of the US policy toward gold:

> After the disintegration of the Bretton Woods system in the 1970s, the gold standard, which had been in use for a century, collapsed. Under the influence of the US dollar hegemony the stabilizing effect of gold was widely questioned; the 'gold is useless' discussion began to spread around the globe. Many people thought that gold is no longer the monetary base, that storing gold will only increase the cost of reserves. Therefore, some central banks began to sell gold reserves and gold prices continued to slump. Currently, there are more and more people recognizing that the 'gold is useless' story contains too many lies. Gold now suffers from a 'smokescreen' designed by the US, which stores 74% of global official gold reserves, to put down other currencies and maintain the US dollar hegemony.

He then goes on to explain how the US is debasing the value of its currency in a move to reduce its mountain of debt:

> The rise of the US dollar and British pound, and later the euro currency, from a single country currency to a global or regional currency was supported by their huge gold reserves. Especially noteworthy is that in the course of this international financial crisis, the US shows a huge financial deficit but it did not sell any of its gold reserves to reduce debt. Instead, it turned on the printer, massively increasing the US dollar supply, making the wealth of those countries

308 Statement made by Prof. Ben Shenglin in 2015.

> and regions with foreign reserves mainly denominated in US dollar (like China) quickly diminish, in effect automatically reducing their own debt. In stark contrast with the sharp depreciation of the US dollar, the international gold price continued to rise, breaking $1900 US dollars per ounce in 2011; gold's asset-preservation contrasts vividly with the devaluation of credit-based assets. Naturally, the more devalued the US dollar, the more the gold price rises, the more evident the function of US gold reserves as a hedge.

Because China had over $1 trillion of US Treasuries in 2010, almost all of which had been accumulated between 2000 and 2010, dollar devaluation would be very negative for China.

So China appears to be up to speed with the underlying reasons for US intervention in the gold market. Additional proof of this can be found in a message[309] leaked by Wikileaks from the US Embassy in Peking about a Chinese newspaper report containing the following text:

> The US and Europe have always suppressed the rising price of gold. They intend to weaken gold's function as an international reserve currency. They don't want to see other countries turning to gold reserves instead of the US dollar or euro. Therefore, suppressing the price of gold is very beneficial for the US in maintaining the US dollar's role as the international reserve currency. China's increased gold reserves will thus act as a model and lead other countries toward reserving more gold. Large gold reserves are also beneficial in promoting the internationalization of the RMB.

309 http://www.zerohedge.com/news/wikileaks-discloses-reasons-behind-chinas-shadow-gold-buying-spree.

Zhang Jie, deputy editor-in-chief of the China Gold Association, also understands the Fed's manipulation of the gold market by storing gold for other nations:[310]

> For the Fed, it is crucial that the dollar dominates the world and so the Fed will store gold reserves from countries all over the world to control the gold settlement system.

310 http://therealasset.co.uk/china-rush-gold/.

91. Everything seems to change suddenly. Is this all part of a greater China plan?

After the start of the financial economic warfare against Russia in 2014 China decided not to join the Western sanctions. China understood that it could well be the next victim of such non-military US aggression and decided to back Russia complete. By joining forces within the BRICS alliance the Chinese took the initiative for a new BRICS bank, the New Development Bank (NBD), a new international payment system, which can be compared to the Western-oriented SWIFT system and the Asian Infrastructure Investment Bank (AIIB). At almost the same time, another important Chinese initiative was launched. The ‘One Belt, One Road Initiative’ (OBOR), a development strategy that focuses on the connectivity and cooperation among countries in Eurasia. It consists of two main components, the land-based ‘Silk Road Economic Belt’ (SREB) and ocean-going ‘Maritime Silk Road’ (MSR).

All these developments within a relative short timeframe underline China’s push to take a bigger role in global affairs. President Xi Jingping seems to be the powerful initiator behind these new initiatives. China has clearly decided to invest portions of its huge financial assets to create an infrastructure that will benefit China and many other countries for centuries to come. So China decided to take advantage of the Western aggression against Russia an agreed on several long term agreements, including huge investments in Energy and railroad projects.

The new infrastructure plans covering Asia and Europe and East Africa consist of two parts:

– Silk Road Economic Belt was announced by President Xi Jinping on a visit to Kazakhstan. This ‘belt’ includes countries situated on the original Silk Road through Central Asia, West Asia, the Middle East and Europe. The idea is to integrate the region into a large economic area through building infrastructure and broadening trade. Many of the countries that are part of this 'belt' are also members of the China-led Asian Infrastructure Investment Bank (AIIB).

– Maritime Silk Road is a complementary initiative aimed at closer collaboration in Southeast Asia, Oceania and North Africa, through trade using – the South China Sea, the South Pacific Ocean and the Indian Ocean. It was proposed by Xi Jinping during a speech to the Indonesian Parliament in October 2013.

The powerful image of the old Silk Road trade route is well known through the marvelous tales of Marco Polo's travels across Eurasia to China. China's development of the world's greatest economic construction project, The New Silk Road, is much more than a revival of this old trade route. It can be seen as part of the battle for dominance in the Eurasian mainland, a great worry for the US. In *The Grand Chessboard: American Primacy and its Geostrategic Imperatives*, a major work by Zbigniew Brzezinski, National Security Advisor during the 1977-1981 Carter administration, his thesis was that no Eurasian challenger should emerge that is capable of dominating Eurasia and thus also of challenging America's global pre-eminence. So China can expect quite a bit of resistance to its ambitious resurrection of this ancient Silk Road, which will connect China, Russia, Europe and Africa in a huge infrastructural system for over 8,000 kilometers. It will create an economic zone that bridges a total population of over four billion people.

The OBOR plan, with its (high-speed) railroads, highways and bridges, will cover almost one third of the earth and will even include fiber optic networks. In China's vision, all countries and cities along the route will benefit from this economic development. The first major development project will take place in Pakistan, where the Chinese will construct, under a long term lease, a deep water port on the Arabian Sea. Thus, the 'New Silk Road' extends a number of already existing projects.

China intends to finance all of this through its newly created Asian International Infrastructure Bank (AIIB), for which China attracted some 60 nations within a year. They will become the founding member and members even include the UK, after failed attempts by the US to persuade allies against joining the bank.

Some understood the significance of these Chinese initiatives right away. The Huffington Post published a story in which they explained:

> For very different motives, the key pillars of the region (Iran, Turkey, Egypt and Pakistan) are re-orienting eastwards. It is not fully appreciated in the West how important China's 'Belt and Road' initiative is to this move (and Russia, of course is fully integrated into the project). Regional states can see that China is very serious indeed about creating huge infrastructure projects from Asia to Europe. They can also see what occurred with the Asia Infrastructure Investment Bank (AIIB), as the world piled in (to America's very evident dismay). These states intend to be a part of it.

92. Does the US feel threatened by these Chinese initiatives?

These developments indicate that a monetary, economic and geopolitical 'reset' process has already started. China clearly wants to cement its regional dominance. The Chinese, like the Russians, clearly want to end the current dollar hegemony and the BRICS alliance wants to compete with the current US-dominated world, with institutions like the World Bank and the IMF. During the annual IMF spring meeting in May 2015, the BRICS Ministers of Finance and the presidents of their central banks held a meeting in which they discussed 'a completely new economic system,' according to reports by the Chinese state press agency.

The Wall Street Journal reported that the US 'had lobbied hard against Chinese plans for a new infrastructure development bank [...] including during teleconferences of the Group of Seven major industrial powers.' China has tried to calm the nerves of the West by stating it seeks cooperation and not confrontation. The news in early 2015 that even the UK would become one of the founding members of the new Asian Infrastructure Investment Bank (AIIB) has shocked many in the West.

Larry Summers, who served as a Secretary of the US Treasury between 1999 and 2001, immediately understood the significance of these developments, and wrote in an op-ed for the Washington Post:

> March 2015 may be remembered as the moment the United States lost its role as the underwriter of the global economic system. I can think of no event since Bretton Woods comparable to the combination of China's effort to establish a major new institution and the failure of the United States to persuade dozens of its traditional allies, starting with Britain, to stay out.

This British announcement was also highly criticized by the US. The Financial Times quoted an unnamed US official:

> We are wary about a trend toward constant accommodation of China, which is not the best way to engage a rising power. This decision was taken after no consultation with the US.

Summers was also critical of the US strategy toward the newly founded AIIB:

> The US misjudged the situation tremendously, put pressure on allies and developing countries to under no circumstances be part of AIIB [...] Largely because of resistance from the right, the United States stands alone in the world in failing to approve International Monetary Fund governance reforms that Washington itself pushed for in 2009. By supplementing IMF resources, this change would have bolstered confidence in the global economy. More important, it would come closer to giving countries such as China and India a share of IMF votes commensurate with their increased economic heft.

With Britain and many more major European countries signing up as founding members of the AIIB, the US economic hegemony has been dealt an enormous blow. For the first time since the end of the World War II, the US is not in the driving seat during the foundation of a highly significant global institution. Of course, this will not change the world economic system overnight, but when we look back in five, ten or even fifteen years' time, March 2015 may be remembered as a turning point in economic history.

93. Is China preparing Plan B or are they pressurizing the US to modernize the IMF, the World Bank and current dollar system?

An analyst once remarked that 'Great powers often don't just want to join other powers clubs, they want to start their own.' While the Chinese have said they want the AIIB to cooperate closely with the IMF, the World Bank and the Asian Development Bank (ADB), the BRICS-oriented AIIB is a clear rival for these US-dominated organizations. Behind all these plans lies the imperative to secure supplies of natural resources and to develop international markets for Chinese products. It is part of the battle for the dominance over Eurasia between the US and BRIC countries like Russia, India and China.

The BRICS alliance understands that a common voice from, in total, over three billion people cannot be ignored or marginalized by the West with less than one billion people.

As mentioned, one of the prime reasons for the establishment of the AIIB has been Chinese frustration with 'the slow pace of reforms and governance in global established institutions like the IMF, World Bank and Asian Development Bank, which it claims are dominated by American, European and Japanese interests.' As Summers has pointed out, all of this has taken place because the Chinese leadership has had to wait a full five years for a change in the IMF voting structure.

The Asian Development Bank (ADB) has published a report stating that the region requires up to $9 trillion in infrastructural investments in the coming years. Although China is the largest investor in the region, it has merely 5% of the voting rights in the ADB, while Japan and US have a total of 26% of the voting rights (13% each). This can be seen as an attempt to keep the Asia investment developments under Western control.

This same kind of US dominance can be found within the voting structures of the IMF and the World Bank. According to some, international politics play an important role in IMF decision making. The most important decisions within the IMF require a special majority of 85% of the votes, giving the US, with over 17% of the votes, an effective veto. France, a country with just over 65 million people, currently has more voting rights (4.29%) within the IMF than China (3.99%) with 1.3 billion inhabitants. Belgium, with just over 10 million people, has more voting rights (1.86%) than Brazil (1.72%), a country with a population exceeding 200 million.

Another criticism is that the US move to more neoliberalism and global capitalism since the 1980s has led to a change in the functions of the IMF. Criticasters claim allies of the US receive 'bigger loans with fewer conditions.' Foreign governments who are non-allies have to sacrifice their political autonomy in exchange for IMF funds and often have to sell assets crucial for their economy to foreign (often US) companies.

The former Tanzanian President Julius Nyerere, who was angered that debt-ridden African states were forced to hand over their sovereignty to the IMF (and World Bank), once asked: 'Who elected the IMF to be the ministry of finance for every country in the world?' And now the Chinese have openly asked for a 'new world wide central bank.'

Joseph Stiglitz, a former chief economist at the World Bank, has also agreed that the IMF 'was reflecting the interests and ideology of the Western financial community.' The 'helpful hand' by the IMF and World Bank toward military dictatorships friendly to the West has been criticized as well.

94. Which currency will the AIIB use?

Of course the AIIB will serve as an instrument of Chinese foreign policy. An article, which appeared in Chinese state-controlled *The Global Times*, denied the notion that China wants a yuan-based global economic system:

> The establishment of the Asian Infrastructure Investment Bank (AIIB) has been depicted by a few overseas media outlets as if China is building its own version of the Bretton Woods system [...] Some foreign observers claim that the AIIB is the beginning of the Chinese yuan's hegemony. What they are actually trying to imply is that 'China is another US'.
> This kind of statement is nonsensical and uses historical experience to fool readers. It is divorced from the truth and shows no common sense and doesn't stand up to any scrutiny. Through the Bretton Woods system, the US was able to wield supreme influence over its allies which had been severely battered during the war. China today is in a totally different position. The AIIB will not confront the WB (World Bank) or IMF, nor will it turn the current international monetary order upside down. The spirit of the AIIB is diversity and justice.

According to other Asian media reports,[311] the AIIB wants to establish an AIIB-currency basket with China set to push for the yuan to take a prominent role. We quote from a report in the South China Morning Post:

> Beijing will push for the yuan to be included in a basket of currencies used to denominate and settle loans from the Chinese-led Asian Infrastructure Investment Bank (AIIB).

311 *The South China Morning Post*, http://www.scmp.com/news/china/economy/article/1766627/china-seeks-role-yuan-aiib-extend-currencys-global-reach.

> Beijing will also encourage the AIIB and the Silk Road Fund[312] to set up special currency funds and issue yuan-denominated loans through both institutions […] there were three options: the yuan, the US dollar or an AIIB currency basket. It said that of the three the US dollar would be the most cost-efficient and convenient, and the yuan the most expensive and least convenient. A currency basket was the most attractive option, it said, because it would be more resilient to market shocks. Hao Hong, chief economist and managing director of research at Bocom International, said the AIIB's grand vision for infrastructure investment came with challenges but China should do its best to establish the yuan as a currency for settlement and denomination. 'If the US dollar is used instead, it weakens China's bid for the yuan to become a truly global currency and to challenge the hegemony of the US dollar.'

According to David Marsh (OMFIF), the New Development Bank (NDB), which was proposed by the BRIC countries in 2014, is a 'clear potential rival to the International Monetary Fund (IMF) and the World Bank.' He wrote that the NDB [and AIIB – WM] represents the biggest challenge to the world monetary establishment since the creation of the Bretton Woods institutions 70 years ago. He thinks the NBD will be 'a renminbi-based institution':

> The credo will no doubt be that 'all currencies are equal' – but the renminbi will be more equal than others. Beijing's long-running efforts to optimise cross-border use of the Chinese currency, especially for trade-linked transactions, and whittle away at the dollar's 'exorbitant privilege', will gain a further boost. On the other hand, the IMF's Special Drawing Right (SDR) – supplemented perhaps by inclusion of the renminbi as well as some of the other countries' currencies – may well be given a role […] [but] the dollar will not be given any prominence in the bank's balance sheet and operations.

312 http://www.asiaasset.com/news/scsilrd_da_2104.aspx.

The BRICS account for 30% of world GDP and houses 45% of the world's population. The BRICS have already started with a huge de-dollarization program in which bilateral 'currency swaps' exclude the need for dollars in bilateral trade. Another important development is the set up of the Shanghai Cooperation Organization (SCO) in which most Asian countries, including Russia, India and China now cooperate. The SCO countries control 20% of the world's oil and almost 50% of the world's gas reserves. It is an important element for the implementation of China's 'New Silk Road Economic Belt' expanding an international railroad network all the way to Germany and the Port of Rotterdam in the Netherlands.

Albert Cheng of the World Gold Council remarked in 2015 that China wants to integrate gold into the One Belt, One Road project (OBOR) in the 'next decade'. The announcement of a Chinese led Gold Fund[313] in 2015 is another indication of a move in this direction. The $16 billion fund, larger in size than all other gold funds worldwide combined, will be active in the field of exploration, development and production of gold in countries, which are part of the New Silk Road project.[314] Song Yuqin of the Shanghai Gold Exchange has stated, 'Asians have a tradition of collecting gold. The gold trade is expected to become a significant component of transactions by 'Belt and Road' countries.'

313 Two top Chinese gold producers Shandong Gold and Shaanxi Gold own together 60% in this fund, which will include a gold ETF and investments in gold miners equities.

314 On 11 May 2015, China's largest gold mining company, China National Gold Group Corporation (CNGGC), announced it has signed an agreement with Russian gold miner Polyus Gold to deepen ties in gold exploration.

95. What is the relation between the AIIB and the Eurasian Economic Union?

In 2014, Belarus, Russia and Kazakhstan formed an economic union called the Eurasian Economic Union (EAEU), on initiative of the Kazakh president and dictator Nazarbayev. He is of the opinion that the dollar is an 'illegal and non-competitive means of payment [...] the world currency was never adopted by any communities or organizations.' Just like China and Russia, Nazarbayev believes the world is heading toward a new monetary system based on a 'non-defective currency'.

In recent years, we have seen the EAEU aggressively expanding and Armenia and Kyrgyzstan are now members as well. Turkey and Vietnam could be next. The current EAEU flag displays the whole of the Eurasian continent, including the eastern part of the Middle East. According to Russian media reports, Putin and Xi Jinping want to tie the development of the EAEU into the Silk Road economic project. The Russian President Putin:

> The integration of the Eurasian Economic Union and Silk Road projects means reaching a new level of partnership and actually implies a common economic space on the continent.

Other Russian media reported the following:[315]

> [...] The partnership's reach is extremely wide, from Russia-China cooperation within the Shanghai Cooperation Organization (SCO) to the Russia-China stake in the new BRICS development bank, and to Russian support to the Chinese-led Asian Infrastructure Investment Bank (AIIB) and the Silk Road Foundation [...] Beijing and Moscow, along with the other BRICS nations, are fast moving to trade independently of the US dollar, using their own currencies. In parallel, they are studying the creation of an alternative SWIFT system

315 http://sputniknews.com/columnists/20150410/1020714196.html.

– which will necessarily be joined by EU nations, as they are joining the AIIB.

According to the former highly respected Indian diplomat Bhadrakumar, this new cooperation between Russia and China is not something to be ignored:

> Clearly, the cold blast of western propaganda against the EAEU failed to impress China [...] China's integration with the EAEU means in effect that a real engine of growth is being hooked to the Russian project. In reality, China is the key to the future of the EAEU. Significantly, [Chinese President] Xi has combined his visit to Moscow with a tour of Belarus and Kazakhstan, the two other founder members of the EAEU [...] This is vital for the implementation of the Silk Routes via Russia and Central Asia.

A 2014 study by the EU Institute for Security Studies explains why Russia is so interested in adding Cyprus or Greece to the EAEU:

> Sergey Glaziev, Putin's advisor on Eurasian integration who seems to have played a key role in the Russian efforts to scupper EU-Ukraine Association in the autumn of 2013, wrote an article in December 2013 outlining the future prospects for the Eurasian Union. His vision includes the idea of inviting some EU member states to quit the EU and join the Eurasian Union. He suggests that 'Cyprus could be used as a pilot project for transition from the European to Eurasian integration. For Greece and Cyprus, it would open new opportunities to boost the export of their goods and services to the market of the Customs Union of Russia, Belarus and Kazakhstan [...] Turkey would be a welcome participant in the Eurasian integration. At this point, the participation of Greece, Cyprus and Turkey in the Eurasian economic integration is unrealistic due to their external commitments to the EU. To accomplish this objective, the first two states must withdraw from the EU,

> while Turkey will have to quit the customs union with the EU. This may entail their expulsion from NATO.[316]

In 2015, during the celebration of the 70th anniversary of the allied victory in World War II, Indian, Chinese, and Russian troops paraded together on the Red Square and China and Russia agreed to tie development of the Chinese Silk Road project to the Russian sponsored Eurasian Economic Union (EAEU). The Russian deputy minister of defense said:

> Moscow and Beijing will seek the reconstruction of the current world order together. […] Our Chinese colleagues have emphasized that we have similar positions on the problem of challenges and threats. They noted the necessity of reconstruction of the current world order, moving away from double standards and strengthening of equal and mutually profitable relations between all countries in the world.[317]

According to the state-controlled Russia Today, the 'military cooperation between Russia and China will be aimed against mono-polar world and double standards.'

The founding members of the AIIB include well over a quarter of the world's nations; 16 of the world's 20 largest economies are on board. Gold seems to be an integral part of Chinese AIIB (One Belt One Road) plan. There have even been some preliminary talks for an EAEU joint currency, the Altyn, which means gold. Not surprisingly, the main countries involved, Belarus, Kazakhstan, Russia and China, have all increased their gold reserves in recent years.

316 http://www.iss.europa.eu/uploads/media/CP_132.pdf.

317 http://rt.com/politics/257821-russia-china-challenges-military/.

Gold Reserves (tonnes)	Q1 2000	Q4 2014
Armenia	1.35	–
Belarus	0.01	42.44
China	395.01	1,054.09
Kazakhstan	56.04	191.79
Kyrgyz Republic	2.58	3.94
Russia	422.60	1,208.19

Source: World Gold Council/Bullionstar

So it seems that this 'push westwards' is China's way of showing that it will be a new global power. US President Barack Obama has even used these developments to defend the Trans-Pacific Partnership (TPP): 'If we don't write the rules, China will write the rules out in that region.'

Since Russia's annexation of the Crimea after the regime change in the Ukraine, China has been careful not to condemn Russia's action. The Chinese have a few good reasons not to be very vocal about Russia new moves. First, it is not in China's culture to behave like the world's policeman. To the contrary, China, just like Russia, would welcome a less aggressive US, telling the world how to behave, mostly inspired by their own (business) interest. China also benefitted from Western sanctions toward Russia. The gap left behind after the many cancelled business contracts with European countries was eagerly filled by Chinese companies.

Putin has proposed that Chinese companies should invest even more in Russia. Surprisingly, he indicated only two no-go areas – platinum and gold. This is another reminder about the unique place precious metals still have. Putin seems to be well aware of the growing importance of gold within our monetary system, also visible in the repatriation (or discussions about this) in at least four European countries.

96. What is Russian perspective on gold?

The Chinese stance can be likened to the position adopted by Russian leader Vladimir Putin. On a number of occasions, he has publicly criticized the privileges the US enjoys in the current system. Speaking at a youth summer camp in 2011, he said:[318] 'They (the Americans) are living like parasites off the global economy and their monopoly of the dollar.' He has called for 'another world reserve currency', and at the 2009 G20 gathering, then President Dmitry Medvedev showed everyone a sample coin for a future goldens world currency.[319]

At the 2004 meeting of the London Bullion Market Association (LBMA) in Moscow, the deputy chairman of the Russian central bank Oleg V. Mozhaiskov delivered a speech in which he accused central banks and bullion banks of being involved in the management of the price of gold.[320] He concluded that the gold market 'may be less than free'. When the Gold Antitrust Action Committee (GATA) requested a copy of this speech, the LBMA refused to release it. When the Bank of Russia learned about this, it supplied GATA with an English translation within a week.

GATA was formed in early 1999 to expose the manipulation of the gold market. At first, the founders of GATA believed the manipulation involved various bullion banks, such as JPMorgan, Chase Bank, Goldman Sachs. It was some time later that they realized the manipulation was far vaster and included the Fed, the US Treasury and other central banks such as the Bank of England. Since then, GATA has always claimed that the yearly gold market deficit was being met by surreptitious selling by central banks.

318 http://www.reuters.com/article/2011/08/01/us-russia-putin-usa-idUSTRE77052R20110801

319 http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aeFVNYQpByU4

320 http://news.goldseek.com/LemetropoleCafe/1330458367.php

While the Western media has ignored these GATA claims, the Russians and Chinese have been very interested in GATA's research.[321] Both countries understand and resent the enormous advantages the US has benefited from, since the introduction of the gold dollar standard in 1944.

During his speech at the LBMA meeting, Mozhaiskov cited GATA's work and explained why gold market manipulation was important to the US likening the central bank to a giraffe, Mozhaiskov quoted a poem well-known in Russia: 'The giraffe is tall, and he sees all.' He acknowledged that the sharp increase in the use of derivatives and the central bank leasing of gold have depressed the gold price in recent years. According to Mozhaiskov, gold is mainly 'a financial asset, not just a precious metal', and due to international financial circumstances, gold and other hard assets were 'more desirable for investment'.

So Russia and China fully understand that the present dollar system is on its last legs and that gold will probably always be a part of the world's monetary system. The old saying 'He who has the gold makes the rules' has been known in the East for thousands of years.

321 According to GATA, three conference calls have been held with the Chinese Investment Corporation, a Chinese sovereign wealth fund, between 2002 and 2013.

97. Could the US confiscate foreign gold holdings?

As always, the future will unfold in a way that we cannot foresee right now. The crucial question is whether an international consensus over a reset of the global financial system can be reached in time.[322]

A breakdown in trust between the most important economic powers could result in a worst-case scenario of escalating trade-, financial- and even real wars, which could include gold confiscations.

There are some who explain China's rush to build up its gold reserves by inferring that the US would prefer to revalue gold together with the EU and China instead of going it all alone. As soon as China's gold reserves as a percentage of GDP reach the same level as that of the US and the EU, the three powers could lead the world in a smooth transition to a system based on SDRs with a form of gold-backing, as proposed by Mundell and the IMF. This scenario is also posited by James Rickards:

> The Fed will do everything they can. When they can't win the battle against deflation, they devalue the currency against gold, cause gold's the only thing that can't fight back. If the Fed wins we'll get inflation and gold will go up. If deflation prevails, we'll wake up one morning and gold will be revalued. The catalyst for a spike into the \$ 2,500 to \$ 3,000 price range will be an announcement by China [...] that they have acquired 4,000 or more in their official gold reserve position. This will put China on an equal footing with the US in terms of a gold-to-GDP ratio and validate gold as the real foundation of the international monetary system. Once that position is validated, gold will move to the \$ 7,000 range [...] Any lower price level is deflationary and must be avoided at all costs by central banks. The key is that the US and IMF do not want gold

322 The US, the European Union and China together represent 60% of the world's GDP.

> to achieve its full potential price (of around $7000) until China has acquired its appropriate share of official gold reserves. Any other outcome is unacceptable to China.

Rickards says he expects the Chinese to 'command a seat at the top table of the central banks. He has also warned that, should there be another dollar panic, the US might not hesitate to confiscate foreign gold holdings stored with the New York Fed in order to introduce a new gold-backed dollar.[323] The introduction of a gold standard by the US could be needed to avoid chaos and regain trust:

> A return to a gold standard is a possibility, but I don't see that in the immediate future, I think we need to have a collapse first. A collapse of the dollar standard and the petro-dollar deal. Then it [the dollar] will have to be replaced with something, which will either be the SDR or gold. By confiscating foreign official gold holdings and private gold on US soil, the Treasury would possess over 17,000 tons of gold, equal to 57% of all official gold reserves in the world. This would put the United States in about the same position it held in 1945 just after Bretton Woods. Such a hoard would enable the United States to do what it did at Bretton Woods, dictate the shape of the new global financial system.

Since the 1930s, countries stored their gold in the US,[324] for fear of a German or Russian invasion during and after World War II. Soon after the financial meltdown at the end of 2008 central banks began to realize the importance of holding gold as a safe haven. Some European central banks stopped selling gold and

323 In his book *Currency Wars.* http://www.itulip.com/forums/archive/index.php/t-23752.html.

324 Stored at the Federal Reserve Bank of New York, not in Fort Knox.

others started to repatriate their physical gold holdings from the US. A former Director of the United States Mint explained:[325]

> Finally, more countries are repatriating their gold. For them, an audit is not enough. They would like their gold back. Azerbaijan, Ecuador, Iran, Libya, Mexico, Romania and Venezuela is a short list of countries that have requests into their custodians to transfer some or all their gold back to their countries.

The repatriation of over 120 tonnes of Dutch gold from New York in 2014 and efforts from the German central bank (Bundesbank) to repatriate 300 tonnes since 2013 demonstrate that this trend of gold repatriations has picked up recently. In France, the leading right-wing politician Marine Le Pen demanded that French gold should be brought back home. She also demanded that France stop selling gold and said that they should use financial reserves to buy more gold and she wants a complete audit of France's 2,400 tons of gold. The national bank of Austria also decided to start a process for the repatriation of their foreign gold holdings in 2015. These gold repatriations by European countries are another sign that we are reaching the end of a calm monetary period of over 40 years.

So we can conclude that gold is making a remarkable comeback into our financial system and even that a new gold standard is being born without any formal decision. At least, that is how Ambrose Evans-Pritchard, an influential international business editor of *The Telegraph*, described the on-going efforts by countries to lay their hands on as much physical gold as possible last year.

> The world is moving step by step towards a de facto Gold Standard, without any meetings of G20 leaders to announce

325 http://www.moneynews.com/Ed-Moy/gold-central-bank-audit-dollar/2014/06/13/id/576839/.

> the idea or bless the project […] Neither the euro, nor the dollar can inspire full confidence, although for different reasons. EMU is a dysfunctional construct, covering two incompatible economies, prone to lurching from crisis to crisis, without a unified treasury to back it up. The dollar stands on a pyramid of debt. We all know that this debt will be inflated away over time – for better or worse. The only real disagreement is over the speed […] The central bank (gold) buyers are of course the rising powers of Asia and the commodity bloc, now holders of two thirds of the world's $11 trillion foreign reserves, and all its incremental reserves. It is no secret that China is buying the dips, seeking to raise the gold share of its reserves well above 2%. Russia has openly targeted a 10% share. Variants of this are occurring from the Pacific region to the Gulf and Latin America. And now the Bundesbank has chosen to pull part of its gold from New York and Paris. Personally, I doubt that Bundesbank had any secret agenda, or knows something hidden from the rest of us. It responded to massive popular pressure and prodding from lawmakers in the Bundestag to bring home Germany's gold. Yet that is not the end of the story. The fact that this popular pressure exists – and is well organised – reflects a breakdown in trust between the major democracies and economic powers. It is a new political fact in the global system.[326]

He also quotes Mohammed El Erian, Pimco's former chief investment officer, who is afraid that the repatriation of gold might lead to a growing international mistrust in our financial system:

> In the first instance, it could translate into pressures on other countries to also repatriate part of their gold holdings. After all, if you can safely store your gold at home – a big if for some countries – no government would wish to be seen as one of the

326 http://blogs.telegraph.co.uk/finance/ambroseevans-pritchard/100022332/a-new-gold-standard-is-being-born/.

last to outsource all of this activity to foreign central banks. If developments are limited to this problem, there would be no material impact on the functioning and well-being of the global economy. If, however, perceptions of growing mutual mistrusts translate into larger multilateral tensions, then the world would find itself facing even greater difficulties resolving payments imbalances and resisting beggar-thy-neighbour national policies.

These developments could have big repercussions, just like the repatriation of gold in the 1960s, which led to the implosion of the London Gold Pool in 1968.

David A. Stockman, a former director of the US Office of Management and Budget who worked under President Reagan in the 1980s, also expects gold to shine again:

> People are going to realize this has been a giant con game, not simply since the bottom in March 2009, but for several decades, and now it's coming to an end. And as even Alan Greenspan had to admit the other day when he appeared before the Council on Foreign Relations, there is another currency out there that is not controlled by the central banks and is not printed at this kind of lunatic rate by the central banks – it's called gold. It [gold] will be rediscovered, and when it's rediscovered as the monetary breakdown gathers force and intensity, the price of gold is going to head upward at a pretty rapid rate.[327]

327 http://kingworldnews.com/kingworldnews/KWN_DailyWeb/Entries/2014/11/15_David_Stockman_On_Monetary_Breakdown_%26_Skyrocketing_Gold.html.

98. Are there any signs of a coming global monetary reset yet?

At the 2014 edition of the Chinese International Finance Forum (IFF) 'a new global financial order has been discussed with China.'[328] This forum, which is not that well-known abroad, is the most prestigious economic conference in China every year.[329]

The IFF Forum points to several 'top priorities' needed to transform the current monetary system:

– establishing new global financial frameworks
– formulating new regulatory systems
– reconstructing new pattern of the world finance

For three days the forum (including UN, World Bank and IMF participants) discussed 'the new framework for the global financial and economic system.'

The *China Daily* reported:

> A new global financial order is essential in the rapidly changing global economy, and strategic dialogues and cooperation are needed to reform the current system, international financial experts said at a forum in Beijing.

Cheng Siwei, chairman of the (IFF) remarked:

> The world today is facing a revolution. It is imperative to construct a new global financial framework and to formulate new

328 http://www.examiner.com/article/finance-experts-call-for-a-new-global-financial-order-at-beijing-conference.

329 The IFF Board consists of Mr. Cheng Siwei as the Chairman; Mr. Paul Volcker as the Honorary Chairman; Mr. Han Seung-soo, Mr. Jean-Claude Trichet, and Mr. Kevin Rudd as the Co-Chairman. The IFF 'is an independent, non-profit and non-governmental international organization and a regular platform for global top-level dialogue and academic research in the fields of finance and economics'. It was founded in 2003 and its members come from China, US, EU and international organizations such as the UN, and a large number of financial institutions.

> rules for global financial market. The new global framework, new global rules, global balance and global governance require us to engage in renewed strategic dialogue and thinking.

Jean-Claude Trichet, former president of the European Central Bank, in his role as a co-chairman of the IFF told the forum via a video link:

> The world has gone through the global financial crisis [...] new rules have been discussed not only inside the advanced economies, but with all emerging economies, including the most important emerging economies, namely, China.

These views were also shared at the LBMA Forum in Singapore. Zhou Ming, General Manager of the Precious Metals Department at ICBC remarked: 'With the status of the US dollar as the international reserve currency being shaky, a new global currency setup is being conceived.

These moves came after the Chinese credit rating agency Dagong downgraded US debt from A to A- in 2013 and China had entered into a very large number of currency swap agreements with dozens of countries, which will result in the decline of dollars used for Chinese trade. In 2014, at the annual meeting of the Bretton Woods Committee, Paul Volcker also proposed working toward a monetary reset.

In a speech titled 'A new Bretton Woods?' he remarked:[330]

> By now I think we can agree that the absence of an official, rules-based cooperatively managed, monetary system has not been a great success. In fact, international financial crises seem at least as frequent and more destructive in impeding economic stability and growth [...] The agreed changes in IMF governing structure are important in achieving a sense of political legitimacy for its governing structure and decision-making. But that is not enough – it means little without substantive agreement on the need for

330 http://www.brettonwoods.org/publication/remarks-by-paul-a-volcker-at-the-bretton-woods-committee-annual-meeting-2014.

> monetary reform and practical approaches toward that end [...] A new Bretton Woods conference? We are long ways from that. But surely events have raised, whether we want to admit it or not, some fundamental questions that have been ignored for decades.

At a conference organized by the Ludwig von Mises Institute in Germany in 2014, Jürgen Stark, former vice president of the Bundesbank and also former chief economist of the ECB, concluded that 'the system is out of control.' According to media reports, he warned the attendees directly against a probable collapse of the global monetary system. He said that the ECB 'has completely lost all ability to control and the economic situation,' and that 'the whole system will not survive [...] it is pure fiction now.' Stark even recommended allocating savings into 'traditional safe havens such as gold or silver.'[331]

During a panel discussion at the World Economic Forum in Davos in early 2014, the IMF's chairwoman Christine Lagarde said it was time to 'move to another monetary policy.' In her prepared remarks she mentioned the word 'reset' more than ten times in a two and a half minute timeframe, as if she had decided to prepare the world for the coming changes in the world wide financial system.

Here are some of her other remarks:

> The financial sector regulatory environment has to be finalized and has to be constantly re-examined, reformed and organized in such a way that it responds to the creativity on the financial markets, that's reset number one.
> Reset number two [...] is a reset of the monetary policies by most central bank of the advanced economies. They've been going into unconventional territories. They've have done a great job at keeping the crisis at the level where it was, but now gradually they're going to have to move to another monetary policy.

331 http://globaleconomicanalysis.blogspot.com/2014/05/former-bundesbank-vice-president.html#ldjHYwcdkYSeQ4mW.99.

In a recent interview, Wall Street insider Jim Rickards also agreed on the need for a global monetary reset. His views can be seen as the American side of the reset card:[332]

> Yes, there is a probability the SDR will be the new global reserve currency. Gold and oil would then be priced in SDRs. It will be used for some of the balance of payments between countries, the creation of reserves and probably the financial accounts of the world's largest corporations. So Siemens, General Electric and IBM will produce their financial statements in SDRs, because they're global corporations [...] they want a paper SDR to replace the paper dollar. The question is, will people go along with that? Our global leaders may have to go back to gold not because they want to but because they need to restore confidence [...] The Fed right now wants the price of gold to be higher. The Fed's problem today is not inflation it's deflation. The Fed wants controlled inflation and they can't get it. So how do you get inflation? You have to change expectations. So allowing the price of gold to go up helps to increase inflationary expectations. It can't go too far too fast, it can't do what we just described. But the Fed wouldn't mind if the price of gold would go to $1400, $1500, $1600 dollars because that would get people into an inflationary mind set; trying to get them spending more dollars, borrowing more, etc. That's what the Fed wants. Where the Fed is wrong is to think that they can just dial it up or down. They did do that in 2011 when gold went to $1900, the Fed was very fearful gold would go to $2000, a big psychological threshold, so they had to push it down [...] I know for a fact that SAFE, which is a Sovereign Wealth Fund that manages the foreign exchanges reserves of the People's Bank Of China, bought 600 tonnes of physical gold through June and July 2013. I know this from the Perth Mint and Chinese dealers. At this moment the gold is on the balance sheet of SAFE but this can be

332 http://www.ingoldwetrust.ch/interview-jim-rickards-on-the-death-of-money.

> flipped to the PBoC's sheet like it happened in 2009[333] [...] China right now has an interest in keeping the price low because they want to buy more. But at some point, if there will be inflation in the US, they want the price to go higher because that's their hedge. That's the reason they're buying gold [...] China has got $4 trillion dollars in reserves, their preference is a stable dollar. If the US devalues the dollar by 10%, that's a wealth transfer of $400 billion from China to the US.[334] China's hedge is gold, if the dollar would go down gold goes up [...] I know wealthy Americans taking measures like getting a second passport and moving their money offshore [...] They're ready for the collapse, but want to milk the system in the meantime.

Another insider who is very vocal about the need for a monetary reset is legendary Hedge Fund manager George Soros. In a television interview he points to the following facts:[335]

> I believe that basically the system is broke and needs to be. The system we now have has broken down, only we haven't quite recognized it. So you need to create a new one and now is the time to do it [...] You need a new world order where China has to be part of the process of creating it. They have to buy in [...] And I think this would be a more stable one where you would have coordinated policies. I think the makings of it are already there because the G20 effectively is moving in that direction [...] So there is a general lack of confidence in currencies and a move away from currencies into real assets. [...] Especially in the area of commodities.

333 In June 2015 the PBoC added 604 tonnes to its official gold holdings. http://mobile.reuters.com/article/BigStory11/idUSKCN0PU0V220150720?irpc=932
334 Only 30% of Chinese financial reserves are in dollar holdings. So wealth transfer should be around $130 billion.
335 https://www.youtube.com/watch?v=uYtdxpLr9Rw&feature=player_embedded&app=desktop.

So we have seen many indications about the coming changes for our monetary system. This does not mean we have to expect a worldwide reset earlier than previously expected. The planned changes in monetary and geopolitical affairs will take time to discuss and to prepare. With the start of the Asian Infrastructure Investment Bank, the new Silk Road initiatives and many other BRIC projects, we could well conclude the global reset has already started. If you are lucky, the effects on your life maybe small but it could turn your life upside down as well.

In my humble opinion, China owns all the keys now and they will do what is in their best interest to reach their long term goals. They will continue to play chess on all boards and to support both Russia (big neighbour and needed for commodities) and the US (worldwide partner for geopolitical and economic reasons). The Chinese leadership understands they need at least another ten to twenty years to improve their own financial and military structures before they can be in a position to compete with the US for worldwide leadership.

But there is a risk that a new crisis will occur before a planned reset could be unrolled and chaos will take over. The US could even be forced to impose martial law or other far-reaching measures to control the public and the economy. As early as 2006, the US[336] government secured a $400 billion contract with Halliburton to set up internment camps spread over the US.[337] These could well be used to detain a great number of US citizens in case of a large-scale revolt as a result of a full market collapse.

336 http://www.in!_niteunknown.net/2011/12/13/obama-administration-was-prepared-to-call-a-bank-holiday-in-2009-video/. Former vice-President Dick Cheney was CEO of Halliburton between 1995 and 2000.

337 http://rt.com/usa/news/psyop-activists-internment-resettlement-526/. http://articles.marketwatch.com/2006-01-24/news/30897064_1_kbr-national-emergency-homeland-security-contract. The manual of 326 pages explaining the running of these 'correctional facilities' can be found on the internet.

99. Do we need to fear more financial repression?

The term 'Financial Repression' (FR) was first employed by McKinnon and Shaw in 1973. Investopedia defines financial repression as 'measures by which governments channel funds to themselves as a form of debt reduction.' One example of FR is holding interest rates lower than the rate of price increases in order to lower government interest expenses.

Economist Carmen Reinhart has identified some other forms of financial repression:

- Strict investments regulations
- Nationalizations (confiscations of pensions)
- Regulation of cross-border capital movements
- Prohibition of certain investment assets
- Special taxes (for the rich)
- Direct interventions ('plunge protection team' Wall Street)
- Haircuts on deposits (bail-in)
- Closure of banks (bank holidays)

Since the beginning of 2003, there has been an agreement between Japan and the US to support financial markets by buying equities. Authorities in Hong Kong have admitted that they supported the Hong Kong stock exchange during the Asia Crisis of 1998. In a 2013 survey of 60 central banks by Central Banking Publications and RBS, 23% said they own shares in listed companies or plan to buy them.[338]

Mohamed El-Erian of PIMCO, the global bond investment management company, acknowledged recently that instances of financial repression are increasing in the US. Support for his analysis comes from an unexpected corner. Ex-Fed Governor Kevin Warsh openly admitted that his former colleagues 'are forced to suppress markets.' Clearly the gold and silver markets fall into this category. This confirms the desperate attempts

338 http://www.bloomberg.com/news/2013-04-24/central-banks-load-up-on-equities-as-low-rates-kill-bond-yields.html.

made by the ruling financial and political elite to maintain the current status quo.

History has shown that the closer we come to a major reset, the more likely it is that forms of financial repression will be activated. The reset of the Cyprus banking system demonstrated that very few of those affected were prepared in advance. Worldwide, a number of countries are preparing legislation in anticipation of the same kind of bail-in as the one in Cyprus. The ongoing limitations for Americans on investing abroad are strong indications that more capital controls will be used in the coming years. US citizens in particular should consider spreading their risks and assets geographically.

Governments in need of cash can use pension funds, as we have seen in many occasions in world history. A recent IMF report[339] is very clear on this:

> The distinction between external debt and domestic debt can be quite important. Domestic debt issued in domestic currency typically offers a far wider range of partial default options than does foreign currency-denominated external debt. Financial repression has already been mentioned; governments can stuff debt into local pension funds and insurance companies, forcing them through regulation to accept far lower rates of return than they might otherwise demand. But domestic debt can also be reduced through inflation.

Or a two-year Treasury note could be become a 20-year bond, as was explained by another IMF paper in 2014:[340]

> Possible remedy. The preliminary ideas in this paper would introduce greater flexibility into the 2002 framework by providing the Fund with a broader range of potential policy

339 http://www.imf.org/external/pubs/ft/wp/2013/wp13266.pdf.
340 http://www.imf.org/external/np/pp/eng/2014/052214.pdf.

> responses in the context of sovereign debt distress, while addressing the concerns that motivated the 2002 framework. Specifically, in circumstances where a member has lost market access and debt is considered sustainable, but not with high probability, the Fund would be able to provide exceptional access on the basis of a debt operation that involves an extension of maturities (normally without any reduction of principal or interest). Such a 'reprofiling' operation, coupled with the implementation of a credible adjustment program, would be designed to improve the prospect of securing sustainability and regaining market access, without having to meet the criterion of restoring debt sustainability with high probability.

The 'war on cash' is another risk. JP Morgan Chase has already been 'restricting the use of cash in selected markets, restricting borrowers from making cash payments on credit cards, mortgages, equity lines and auto loans, as well as prohibiting storage of cash in safe deposit boxes', according to a media reports.[341]

A Swiss pension fund, SNB's, has been in discussion with its bank following negative deposit rates. The fund manager calculated that he would save 25,000 CHF per year on every CHF 10 million deposit by putting the cash into a vault. But his bank refused to make that withdrawal possible. Withdrawing cash was regarded as 'interference with the SNB's monetary policy goals.'

In a recent study, the Liechtenstein-based asset management company Incrementum dived a little deeper into this subject, under the title 'The War against Cash';[342]

> As a result of global low interest rate policies, traditional savings vehicles, especially savings accounts, have become less and less attractive. Since they earn practically no interest anymore, there is a growing incentive to withdraw money

341 http://www.zerohedge.com/news/2015-04-25/war-cash-migrates-switzerland.
342 http://www.incrementum.li/wp-content/uploads/2015/06/In_Gold_we_Trust_2015-Extended_Version.pdf.

from bank accounts and hoard it. In recent months especially, another facet of financial repression is increasingly gaining momentum: numerous (supposed) star economists, including the likes of Paul Krugman and Larry Summers, are currently overtly propagating the opinion that too much is being saved and not enough is being invested. In order to compensate for this imbalance, interest rates should be pushed into negative territory. According to Keynesian logic, this will supposedly boost consumption and provide urgently needed stimulus to the economy. In order to be able to implement negative interest rates, Larry Summers, Harvard economist and former US treasury secretary, bluntly demanded the global abolition of all cash currency at an IMF research conference. His presentation gave the impression of being a declaration of war against cash. The primary goal according to Summers should be to enable governments and banks to push interest rates below the level of zero. Consequently, every saver would then have to pay a fee for the warehousing of his money. In order to prevent a run on banks, cash would have to be completely abolished.

Other economists are making similar arguments. Kenneth Rogoff (*'Paper money is the decisive obstacle standing in the way of further interest rate cuts by central banks. Banning it would be a very simple and elegant solution to this problem.'*) and Willem Buiter, chief economist of Citigroup, are also pleading in favor of the abolition of cash. Without cash, it would no longer be possible to escape negative interest rates, and one would finally be able to 'boost' the economy. Even though the idea is controversial according to Buiter, and there are a number of drawbacks (resistance of the population, high rates of cash usage among poor and elderly people, loss of seignorage income of central banks and governments, loss of privacy and security risks due to cyber-attacks), these disadvantages are 'negligible'.

However, the criticism of cash has an additional background: due to tiny minimum reserve requirements, banks are in a permanent state of 'latent illiquidity'. Deposits are the base of the fractional and massively leveraged credit pyramid. A bank run due to a loss of confidence would quickly lead to a collapse of this credit pyramid. Banning cash currency is therefore the only effective tool the 'junta of paper money jugglers' has at its disposal to block all escape routes from the paper money system for the citizenry. The emergency exits would thus be locked down. Moreover, in a cash-less society, assets could be more easily monitored, controlled, taxed and if occasion demands, expropriated. This final factor is seen as ever more essential for governments which are buried in debt up their eyebrows. Restriction of cash holdings thus represents a major pillar of financial repression and moreover the last hurdle prior to the possible introduction of negative interest rates.

Numerous examples show that the path toward the abolition of cash is already pursued:

- In Italy, Spain, and Greece, the possession and use of cash has already been significantly restricted. Since 2011, it is illegal in Greece to perform cash payments exceeding EUR 1,500. In Italy, this limit stands at EUR 1,000 and in Spain at EUR 2,500.
- Denmark wants to abolish the legal obligation to accept cash.
- In France, legal cash payments will be limited to EUR 1,000 from September 2015. Moreover, currency exchange offices are obliged to store the personal data of anyone engaging in foreign exchange transactions exceeding EUR 1,000. Purchases of gold also have to be reported to the authorities from now on, as well as gold shipments within the country, which curiously have to be reported to customs. As one might expect, the measures are justified by invoking the 'war on terror'.

100. What is your advice to investors?

The risks involved with holding a significant portion of personal wealth within the framework of conventional banking and securities arrangements is increasing. Authorities will soon decide that conventional levels and methods of taxation no longer suffice. We can expect new measures to help recapitalize the system such as the 'IMF's one-off capital levy, Cyprus's bank deposit confiscation, or outright sovereign defaults.'

Everything within banking and securities institutions (paper assets) are 'visible forms of wealth'. Tangible (hard) assets are less visible and therefore less vulnerable to broad edicts targeting private wealth.

During the crisis of 2008, policymakers reacted ad hoc but now they have had much more time to plan well-orchestrated responses for a new crisis.

Even the Norway Sovereign Wealth Fund unveiled a new strategy to buy real estate and stocks instead of bonds. The $900 billion oil fund is buying stocks as a safe haven, because governments just like money and sovereign bonds cannot print shares of good companies. The oil fund already owns 2.5% of every listed European company and wants to grow this towards 5% of almost every European listed company.[343]

Gold fund manager John Hathaway believes holding physical gold is the safest type of investment at this moment in time:

> When the market reverses, the diminished physical anchor to paper claims, concerns over title and encumbrances on central bank bullion, and worries over the drift of public policy will drive liquid capital into gold. However, this time around, it seems to us that the major recipient of flows will be the physical metal itself. Holders of paper claims to gold will receive polite and apologetic letters from intermediaries offering to settle in

343 http://www.zerohedge.com/news/2014-06-24/norway-sovereign-wealth-fund-unveils-new-strategy-buy-5-every-european-stock.

> cash at prices well below the physical market. To those who wish to hold their wealth exclusively in paper assets, implicitly trusting the policy elites to resurrect normally functioning capital markets and economic conditions, we say good luck. For those who harbor doubts on such an outcome, we say get physical.

I would like to add that physical silver is an even better investment. At the moment of writing (summer of 2015), gold is over 75 times more expensive than silver. Historically, the norm has been ten to 15 times. Given the growing shortages in the silver market I expect an enormous re-rating of the 'poor man's gold'.

Since 2007, I have stuck to my general model portfolio, which is really quite simple:

- 25% cash
- 25% precious metals (gold/silver)
- 25% real estate (mostly your own home)
- 25% equities (good 'hard assets')

This portfolio has weathered all storms well, since the start of this credit crisis. It is my personal insurance against any possible scenario.