Written by Charles Scaliger on August 19, 2011

Forbes: Time to Re-open the Gold Window

And now this. After 40 years of a “new normal,” the nations of the West are exhausted and bankrupt. Debt in Europe and the United States is spiraling out of control while economies stagnate, and all central bankers can think of is what they’ve been doing since the Nixon years (and, in truth, a lot longer than that): print more money.

No less an authority than *Forbes* magazine has passed verdict on our 40-year experiment with fiat money and undiluted inflationism, calling it Nixon’s “colossal error.” Noting that Nixon promised that emancipation from the gold standard would allow policymakers at the Fed to enhance America’s prosperity and economic growth by manipulating the money supply, *Forbes* expended considerable ink looking at the Fed’s 40-year track record:

> Since Nixon killed the gold standard, the unemployment rate has averaged over 6% and we have suffered the three worst recessions since the end of World War II. The unemployment rate averaged 8.5% in 1975, almost 10% in 1982, and has been above 8.8% for more than two years, with little evidence of any improvement ahead.
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> This performance is horrendous compared to the post World War II gold standard era, which lasted from 1947 to 1970. During those 21 years of economic ups and downs, unemployment averaged less than 5% and *never* rose above 7%.
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> Growth, too, has slowed. Since able men and women were given the power to manipulate the quantity and value of the dollar, real economic growth has averaged 2.9% a year — more than a full percentage point slower than the 4% growth rate during the post World War II gold standard era.
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> A 1% difference may not seem like much, but in reality it is the difference between prosperity and austerity. A growth rate of 3% creates just enough jobs for all new workers. A growth rate of 4% yields higher employment and a decline in the unemployment rate.
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> In addition, when compounded over 40 years, 1% slower growth under the paper dollar system has had a mind-boggling impact on all things that depend on the overall size of the U.S. economy. At 3% growth, the U.S. economy is about $8 trillion smaller than it would have been had we continued to experience the average growth rate prior to Nixon severing the link between dollar and gold. That implies that median family income today would be about $70,000, or nearly 50% higher than it is today.

Moreover, *Forbes* noted that the dollar has fallen more than 70 percent relative to the Japanese yen and the German mark/euro, and 1971's modest trade surplus has turned into a more than $400 billion trade deficit.

Nixon and his cronies promised at the time that the dollar's valuation of 1/35 of an ounce of gold would be maintained; had that happened, *Forbes* pointed out, a barrel of crude oil today would sell for less than $2.50.

The inflationary dollar has placed America on a footing of permanent financial crisis, which Americans have come to accept as normal after two generations. But the record is sobering:

> Since Nixon killed the gold standard, the world has suffered from 12 financial crises, beginning with the oil shock of 1973 and culminating in the financial crisis of 2008-09 and now the debt crisis in Europe, and the growing deficit crisis in the U.S. Conversely, between 1947 and 1967, there was only one currency crisis, involving the British pound, and no major bank failures or Wall Street and corporate bailouts in the U.S.
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> The evidence is in. The great experiment of a paper dollar managed by able men and women has failed and failed miserably to keep any of its promises.

Admirably, *Forbes* calls for a restoration of the gold standard as a long-past-due panacea for at least some of our economic woes. And while such sentiments from a major business magazine like *Forbes* are long overdue, there are a couple of points worth considering. First, Nixon did not abolish the gold standard as it had existed from the founding of the country until the 1930s; he abolished the gold *exchange* standard which had existed since the end of the Second World War. This system did not allow ordinary American citizens to own gold coins, bullion, or certificates (a freedom that was not restored until 1974 by President Ford), or to redeem Federal Reserve notes in gold. That privilege was reserved for foreign holders of U.S. dollars only. This elitist "gold standard" was similar to that imposed on the peoples of Europe after World War I.

Over the past several years, a number of establishment voices have called for a return to the gold standard, but what they usually mean is the gold *exchange* standard, which would once again allow foreigners — but not Americans — to receive gold for dollars at a fixed rate. While such a standard would, by imposing considerable restraints on the power of the Fed to manipulate the money supply, certainly be preferable to no gold standard at all, it would still be a far cry from the liberty to use gold (and silver) for money that Americans enjoyed before the Great Depression (silver coins continued to be minted in the United States until 1965).

It's also worth noting that a return even to a full gold standard would not completely eliminate inflation or the business cycle. After all, a number of panics and other economic crises occurred before the gold standard was abolished, including the onset of the Great Depression itself. These were the consequence of the inflationary activities of fractional reserve banking (i.e., creating and pyramiding new money atop reserves worth only a fraction as much), a practice much older than modern inflationism. Any creation of new money not backed by full reserves produces a malinvestment boom that will eventually go bust. Eliminating such practices will require reforming several centuries' worth of banking laws.

But under a full gold standard, bankers' shenanigans are always corrected fully, rather than being concealed (and their effects palliated) by printing more money. Though the gold-standard economy of the 19th and early 20th century had its booms and busts, the dollar's value was preserved. A suit was worth roughly the same in 1800 as in 1900, and savings accounts kept their value.

Restoring a genuine gold standard would not solve all of our financial problems. But it would be a gargantuan first step in the right direction.