Retirement Lifestyle Advocates

RADIO PROGRAM

Expert Interview Series

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Dennis Tubbergen:

Welcome back to RLA Radio. I'm your host, Dennis Tubbergen. Joining me once again today is the head of research at Gold Money, Mr. Alasdair Macleod. You can actually read Alasdair's work, which I would encourage you to do, at goldmoney.com. There's an Our Research link that you can click on, and Alasdair's articles are posted there. Alasdair, welcome back to the program.

Alasdair Macleod:

That's my pleasure, Dennis.

Dennis Tubbergen:

So, Alasdair, last time you were on, which has been about four months or so, you made the prediction that you thought we were going to see at some point, the end of Fiat currencies and we would likely see a hyperinflation. You can correct me if I'm misstating anything. Is that still your view?

Alasdair Macleod:

Yes, it is. Obviously, this is not something that happens overnight, but I think we can probably agree that there is evidence that we are drifting in that direction.

Dennis Tubbergen:

So, Alasdair, when you take a look at here in the United States, for example, we've had two quarters of negative economic growth. To what extent would you say that the monetary policies are to blame for this official recession, even though we're not supposed to call it that?

Alasdair Macleod:

Well, obviously very much so, and it's not just monetary policy, but it's the whole business of intervening, government intervening in private sector activities. I would also say that the point about GDP, is that actually it's just a record of the total amount of credit in the economy or in the economy to the extent it qualifies on spending and production of the goods, which are included in GDP.

Alasdair Macleod:

It doesn't tell you anything about how that credit is actually used, whether it is used productively or not productively. The important thing is, is that word credit, because what it means is that GDP is actually tied to the bank's willingness to increase their lending. Now, if the banks turn around and decide that their balance sheets are over geared, or the amount of risk in their lending books has increased, then they will tend at the margins to reduce their outstanding lending. Now that inevitably leads to a fall in GDP.

Alasdair Macleod:

So, the thing we need to watch is not so much what's going on in the economy to try and predict the course of GDP, but what's actually happening in the credit markets. I think this is a very important point, which nobody in the investment industry, and I don't think even in the central banks really fully understand, it is a very important point and there are implications that flow from that, obviously.

Dennis Tubbergen:

So, Alasdair, it's a terrific point and I think it's a perspective from which again, most analysts don't look at things. So just talk a bit if you would, about what's going on in banking as far as the credit markets go, over the past couple years.

Alasdair Macleod:

Yeah, sure. I mean, over the past couple of years, we've seen a massive expansion in the quantity of broad money, narrow money as well. Now, a lot of this is put down to COVID. Sorry, excuse me. Certainly, banks have found themselves in the position that if they called in loans, then with business having virtually ceased, I mean, basically their customers would go bust and they wouldn't recover anything from their loans.

Alasdair Macleod:

So, you can see that there was a great disincentive for the banks to reduce their overall levels of credit. Particularly when governments around the world, I don't know the exact detail in America, but certainly here, the banks were given government guarantees behind loans, so that businesses would not be forced to go to the wall. So that I think is the background. Now that has created an inflation problem, which is now leading to rising interest rates.

Alasdair Macleod:

Now, when you get very low interest rates, then the way the banks make money or increase their profits is basically by increasing the leverage on their balance sheet. Why? Because the difference between what they lend it out to and what they have to pay depositors actually narrows. So, they need to have more assets on their balance sheets in order to increase profits at the shareholder level.

Alasdair Macleod:

Consequently, when interest rates start rising, then they have a natural inclination to start reducing their balance sheets. So, what we have got is we've got the situation where post COVID government guarantees are basically being withdrawn from most banks. We've got rising interest rates, which is also undermining the value of bank collateral, where it is held in the form of financial assets. So, everything is beginning to go against the banks.

Alasdair Macleod:

What was very interesting was that I think it was in the very beginning of July. It might have been in the last week of June, Jamie Dimon stood up at a banking conference in New York and said that two weeks before he said that the economy faced stormy weather. "I'm upgrading that," he said, "To hurricane force." Now that is a very important message because Jamie Dimon is the most important banker in the world. I mean, commercial banker, I mean, in the world. This is very, very important.

Alasdair Macleod:

What he's saying is that his bank is not going to take on more risk. It cannot take on more risk. You could go further and say, at the margins that obviously, that his bank is obviously going to reduce the amount of bank credit risk. So, he's likely to contract JP Morgans overall obligations. On top of that, because he is the most important banker in the world, every other banker who was sort of aware of what he said, if they hadn't actually arrived at the same conclusion themselves, which they almost certainly would've done, would've taken note, and this is a very, very bearish development.

Alasdair Macleod:

It's not often we get a very clear signal that the whole of the banking system is looking to reduce its balance sheet, which basically feeds into GDP. So, we get a reduction in GDP. I think we've only just seen the start of it. This is something that could be particularly severe because if you look at the makeup of credit markets in the United States, credit from the central bank in the form of bank notes is only 10% of the money in circulation. So, what we're talking about is 90% of the money in circulation being bank credit, if that begins to contract in a meaningful way, then there is going to be a slump. So, the two quarters that you mentioned, I think are just the start of something, which is likely to be considerably more severe.

Dennis Tubbergen:

So, Alasdair, you just said a remarkable statistic. I always learn something when I talk to you, and today is no exception. When 90% of the currency in circulation is actually bank credit, when you look at all the currency in circulation, as this starts to contract, I mean, we're going to be looking at something that is really depression level, aren't we?

Alasdair Macleod:

Yes. I mean, that is certainly a likely outcome and is the risk, which I think that increasingly central bankers are worried about. It rather explains some of the things that seem to be going on in the background, because we have got, I think, a coordinated effort by the major central banks to try and calm down the inflation story, because they're worried that if they have to raise interest rates further it's just going to tip the whole of the commercial banking system, definitely into contracting the amount of credit that it offers the overall economy.

Alasdair Macleod:

So, we are seeing this now. We've seen bond yields fall fairly, fairly steeply. This is despite the fact that with interest rates, I mean, you've got fed funds rate is standing, I mean, they keep on changing it. So, I can't remember what it is, but it's around about 2% or something or two and a half percent. You've got inflation measured by the consumer price index, running it just under 10. This is still far too large a gap to stop the falling purchasing power of the dollar.

Alasdair Macleod:

The dollar will continue to lose its purchasing power. What's happening is that it's not just the dollar, every other currency is as well. Other currencies have got even greater problems. If you look at the situation with the Japanese yen, for example, the Bank of Japan has taken on enormous quantities of government debt on its own books, as well as even equities through exchange traded funds. Consequently, the bank cannot afford to see bond yields rise, which basically means that the mark to market value of the assets that has been accumulating since the year 2000, it goes down the pan. The same with the ECB.

Alasdair Macleod:

I calculated that at the beginning of last month, the ECBs balance sheet losses were probably in the region of 750 million, sorry, billion euros. Now that's against a level of equity capital in the whole Eurosystem of 109 billion euros. So, they're almost seven times under water. The Bank of Japan I think is probably considerably worse, but this is the sort of problem we have. We've got central banks, which on rising interest rates are effectively insolvent, having to underwrite the commercial banking network, which is running into the same problem.

Alasdair Macleod:

This is a major, major problem, which we have to try and find some way out of. I think the central banker's means of trying to get out of this is to try and dissuade us that prices are going to continue to rise. Now, I think we've then got to look at the geopolitical situation because all that is entirely dependent really on whether Mr. Putin manages to push up energy prices much more. I think that is bound to be something that he regards as being in his armory.

Dennis Tubbergen:

Well, Alasdair, we're sneaking up on the end of a segment already. For our listeners maybe that are not familiar with Gold Money and the kind of work you do, we've got about a minute and a half left for a brief commercial, if you'd be so kind.

Alasdair Macleod:

Oh, that's very kind. Thank you, Dennis. Well Gold Money basically stores precious metals for customers outside the banking system. We offer a range of fully insured vaults around the world. So, you can live in one place, store your gold, silver, or platinum group metals in another place. I basically write the research for Gold Money. I publish research every Thursday and I do a market report on Friday.

Alasdair Macleod:

So that's roughly what we are. The gold and silver and platinum group metals, which we hold for our customers are all off balance sheet. It's all custodial arrangement and it is outside the banking system. So, most of our customers, I think see this quite rightly as being a means of insulating themselves from the potential troubles of a Fiat currency system, that when the risks in that Fiat currency system appear to be rising.

Dennis Tubbergen:

Well, my guest today is Mr. Alasdair Macleod. He is the head of research at Gold Money. I'll continue my conversation with Alasdair when RLA Radio returns stay with us.

Dennis Tubbergen:

I'm Dennis Tubbergen. You are listening to RLA Radio. I have the pleasure of chatting today with Mr. Alasdair Macleod. Alasdair is the head of research at Gold Money. You can learn more about his work at goldmoney.com, and you can click on the Our Research tab to read his articles.

Dennis Tubbergen:

So, Alasdair, just to kind of continue where we left off in the last segment, you stated that really there is in your view, a coordinated effort to kind of calm down the inflation story and dissuade us that prices are going to continue to rise. As you said that it just seemed to me that if you're trying to control the narrative versus correcting the underlying problem, it may seem that this whole situation is too far gone to actually control the problem. Am I reading that correctly?

Alasdair Macleod:

Yes. I believe you are. It's difficult to know how central banks can actually deal with this because they don't actually have the mandate to deal with the problem properly. What they should do is basically stop intervening and let markets set the rate. But the problem is that if the market sets the rate, then not only are commercial banks in trouble, not only are all the malinvestments, in other words, companies that have borrowed money on the basis that it's cheap rather than productive, they're also all in trouble. The central banks themselves are in trouble.

Alasdair Macleod:

So not only do they not have a mandate to actually address this problem, but if they did address it, they would probably threaten their own existence. So, yeah, I mean, I can't really see that there's a sensible way out of this. It's always a case of crisis first, solution second. Unfortunately, I think the crisis that we now face is potentially a lot more severe than anything we have seen since the Wall Street crash in 1929 to 1932, and the aftermath of that in the 1930s.

Dennis Tubbergen:

So, Alasdair, when you take a look at the fed's policy, they just raised interest rates three-quarters of a point at their last meeting. The last time they tried to do this, their balance sheet was a lot smaller. When the economy and the markets started to react negatively, they chickened out. They reversed course. I have said that I think they're going to have to do the same thing again, because they don't really have another tool that they can use. Do you agree with that?

Alasdair Macleod:

Yes, I do. I think the point you make is absolutely right. I mean, really you are talking about the time between, well, particularly between September 2019 when the repo market failed, some of your listeners may recall that and February 2020. During that time, I mean, we forget that the S&P actually lost fully one-third of its value. It collapsed into March 2020, and it was only then that the fed reversed course.

Alasdair Macleod:

Instead of tightening it reduced, well, it had actually begun to reduce interest rates over fed funds rate, but it reduced it to zero, which was unprecedented, and instituted QE of 120 billion a month. I have no doubt that as these conditions move towards a replay of that situation, that any idea of quantitative tightening will be abandoned. We will again get quantitative easing. What this means is, the inflation machine just cranks up again.

Dennis Tubbergen:

So, Alasdair, how does it end? Are we headed for this reset, where people lose confidence in the currency? Are we headed for Weimar, Germany? How does it play out?

Alasdair Macleod:

What I see in this situation is something which is very similar to what happened in France in 1720. I have repeated this several times, but it's worth noting that John Law, who was the sort of prototype of Keynes with his policies, basically puffed up the Mississippi bubble as a means of trying to generate not only income for the state in the form of the king, but also to stimulate the economy. That's what he believed, which actually is pretty much the same as John Maynard Keynes's approach to these masses.

Alasdair Macleod:

What happened basically was that he started debasing the currency to support the asset prices. The asset price predominantly being his Mississippi venture. Now, this is exactly what all the central banks around the world are doing. They're puffing up their markets. They're trying to maintain financial asset values by printing currency and encouraging the expansion of bank credit. What you're seeing is instead of it necessarily going direct into circulation, it's going into pension funds and insurance companies, and then dribbling out into the economy in that way. But nonetheless, it is inflationary.

Alasdair Macleod:

The lesson from John Law was he failed to maintain his Mississippi bubble that burst on him and the currency within a matter of months was completely valueless. His paper currency, the French livres. So, we really have a lot of similarities with that today. The difference today is that we have central banks and multiples of it rather than just one central bank. I think that the real dangers are from the Eurosystem. The Eurosystem, I think will not take very much to make it collapse.

Alasdair Macleod:

If we get rising bond yields again, then there is no doubt in my mind that these highly overleveraged banks in the commercial network, the Eurozones commercial network, they will start failing. The Eurosystem, which is comprised of the ECB and all the national central banks, will have a problem on their hands trying to take on board all the failures in their national networks, commercial networks, while at the same time, they are demonstrably insolvent.

Alasdair Macleod:

They will be insolvent because the bond yields, with higher bond yields, the bonds which they have bought as a result of trying to stimulate the Eurozone economy, will fall in value. As I say, at the beginning of this month, or sorry, last month, because it's the 1st of August, the situation was already seven times the Eurozones, sorry, the Eurosystem's equity, been wiped out about seven times. Now, it's not quite so bad now because yields have fallen a little bit. So, the prices of their bonds will have rallied.

Alasdair Macleod:

You can see how a complete collapse of the Eurosystem is likely to undermine the whole of the Fiat currency system. We don't know how it'll play out, but there is no doubt in my mind that London will be taken out by that because we do all the clearing for the Eurozones commercial banking network. That's all done in London. We have enormous exposure also through our own commercial banks.

Alasdair Macleod:

Less so, America has less of a problem, but the problem is if you take London out, it takes out all the other currencies as well, because we're the main settlement system for international currency trading. So this is potentially something which I don't think we have ever seen before. So I'm very, very cautious about the future. I would take a very, very conservative view when it comes to one's own finances, about exposure and so on and so forth. That's why I think that gold is probably a sensible thing to have because it gets you out of the Fiat currency system as much as possible.

Dennis Tubbergen:

So, Alasdair, I know there's a lot of listeners that are probably wondering, why is it we've got these sobering facts, these are just remarkable things to listen to. Yet when you look at gold prices, you look at silver prices, they haven't reacted as one might have expected them to react. How do you square that?

Alasdair Macleod:

Well, I so often get asked this question and I think there are several answers. The most important ones of which are, I think that the whole of the investment establishment, if I can put it that way is basically driven by Keynesian economic theory. Keynesian economic theory denies the idea that gold is your risk-free asset. The risk-free asset in the Keynesian system is US treasury bonds, probably with a short duration.

Alasdair Macleod:

If we're looking at really the Fiat currency system against a proper sound money system, then there is no doubt about it. Gold is what you should be having, but it's just not recognized by the investment establishment. That's the first thing I would say.

Alasdair Macleod:

The second thing I would say is that the investment establishment in this form, I mean, bullion banks are short. In other words, they have sold paper, gold paper, silver paper, platinum group metals, and they need to cover those positions. So, they will always encourage a fall in the metals prices so that they can make profits. So that's the second thing.

Alasdair Macleod:

I think if you look at history and you look at commodity prices priced in gold, actually what you see is the volatility is not in the gold price. It's actually in the currencies. This is really a quite remarkable discovery because just look at a chart of the oil price in dollars, compare it with gold. Since 1950, the price in dollars has gone up from, I think it's something like $2.68 a barrel, to currently we're trading at about $94 a barrel. In gold, the price has merely fallen by about 30%. That is all.

Alasdair Macleod:

Now that is a remarkable record of stability, pricing oil in gold. I think that's something which with the declining Fiat currency system, I think increasingly oil exporters around the world and particularly, I mean, in Asia, they will be looking I think more and more towards having something like gold to be paid in rather than declining Fiat currencies. We can see already that the petrodollar is actually past its sell by date.

Dennis Tubbergen:

So, Alasdair, last question, do you see the world returning to some type of gold exchange standard currency system?

Alasdair Macleod:

Well, it should do, Dennis, but I think that the root to that solution is going to be fraught with all sorts of misconceptions, politics, geopolitics. To see this sort of sensible return, I think is very unlikely. Now having said that if we get the sort of crisis, which I believe is in the wings, then people's attitudes will change very, very sharply. Now insofar as you can have political stability, they could well move towards the right conclusion. I think in many nations there is unlikely to be political stability, as a result of this, the consequences of such a slump and collapse in currency purchasing powers.

Alasdair Macleod:

That being the case, we're already seeing this. I mean the Dutch farmers are revolting. The Italians as usual. I mean, they don't like their government at all. You can see that on the continental Europe, there are all sorts of political problems being stored up. I would be very, very surprised if we get through some sort of crisis on the scale that I've been talking about without major political disruption, changes, revolutions even in some countries.

Alasdair Macleod:

This is not going to be an easy time, Dennis. It's going to be a very, very difficult time and the move towards proper goldback currencies, I think is not going to be a straightforward question of suddenly they've seen the light. No, I think there's going to be quite a lot to go, to wade through before we get to that point, if we ever do.

Dennis Tubbergen:

Well, my guest today has been Mr. Alasdair Macleod. His company is Gold Money. You can read his research at goldmoney.com and click on the Our Research tab. Alasdair, a half hour with you goes by so fast. I very much appreciate your time. I know you're a busy guy and the listeners always enjoy having you on the program. Love to have you back down the road and thanks again for joining us.

Alasdair Macleod:

That's very much my pleasure, Dennis. Thank you for having me on.

Dennis Tubbergen:

We will return after these words.