Retirement Lifestyle Advocates

RADIO PROGRAM

Expert Interview Series

Guest Expert: Alasdair Macleod
Gold Money

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Dennis Tubbergen:

Welcome back to RLA Radio. I'm your host Dennis Tubbergen. Joining me once again on today's program is returning guest Mr. Alasdair Mcleod. You can read Alasdair's work at goldmoney.com. You can click on the Our Research tab, and Alasdair's work is work that I follow regularly and I'll encourage you to do the same. And Alasdair, welcome back to the program. Always a pleasure to have you on.

Alasdair Macleod:

It's my pleasure, Dennis.

Dennis Tubbergen:

So, Alasdair, I just finished an interview within the last few weeks with a guest who seems to think that the Federal Reserve here to talk about the United States Central Bank understands that they cannot continue to inflate or create currency, whatever term you want to use. And he is projecting that we will morph into a deflationary depression next year. I think that's not quite how you see things. So, could you respond please?

Alasdair Macleod:

Yes. I wouldn't try and demolish his argument on the basis that there is no doubt in my mind that bank credit has started to contract. Now, the importance of bank credit is that all GDP transactions are settled in bank credit. So, if you get contracting bank credit, then you're going to get contracting GDP. So quite simply, there is that relationship. And if I'm right and we're getting contracting bank credit, then obviously the Fed has a problem because it will have to somehow try and accommodate dealing with a recession while at the same time dealing with price inflation. And I think that the contraction in bank credit could be sufficiently severe to bring about that real recession, a deep recession, which of course the Fed will then try to counter. So, it's likely to pivot with QE and also to try and soft pedal on the interest rate side as much as it can, so long as it is not overtly inflationary.

But at the end of the day, I think the Fed is faced with a simple choice. Does it save the economy, and save government finances, and save the markets and let the currency slide, or does it protect the currency and let markets slide, let the economy slide, and let government financing go to pot. I think, I mean, my view on this is that the choice the Fed will make at the end of the day will be to protect the economy, protect government finances, and try and support markets. So, I would see the result of this situation being actions, which will lead to a weakening of the dollar. And of course, we've got the same problem in all the other currencies. So, this may not be reflected as such in the foreign exchanges, but it is likely to be reflected in resurging price inflation, particularly in commodities led by gold and silver.

Dennis Tubbergen:

Alasdair, so essentially the Fed has another problem, and I guess it's related in that borrowing costs for the US government as inflation has come up are now consuming an ever-greater percentage of tax revenues. And a recession of course means that tax revenues contract. So, doesn't this create problems on a lot of fronts, not only for the currency but also for government programs and government spending?

Alasdair Macleod:

Yes, it certainly does. And that's why I think that the Fed will... If it's not under sufficient pressure to do so, it will tend to try and support the situation where government funding, if you like, isn't threatened too much. And the only way it can do that is by continuing to suppress interest rates below where they really should be to reflect the loss of purchasing power of the currency. So, I can see that emotionally the Fed is going to try and keep those boring costs down as much as it can. But the problem is that if it does that, then it is going to sacrifice the currency.

Dennis Tubbergen:

So, assuming they make that choice, Alasdair, and they decide to sacrifice the currency and the dollar, and as you mentioned, this is not just a US problem, this is a worldwide problem, but continues to lose absolute purchasing power. Well, what does this end game look like in your view?

Alasdair Macleod:

Well, the end game looks to me like we are coming to the end of the phase from the end of Bretton Woods when we had the last vestiges of a link between gold and the dollar and through the dollar to other currencies. That phase is now come to an end. And the turning point I think is marked by a change in trend in interest rates which have been driven by a resurgence of price inflation. And the price inflation was really triggered by an excessive expansion of the quantity of credit in the economy as a response to the COVID crisis.

And of course, that has been exacerbated by actions on the political front, sanctions against Russia, which has had the effect of driving up energy prices and food prices, which are the most important elements of any, if you like price index because those are the things that people actually require to live on. They don't need to buy a lot of the other things in the index, but the two things they really do need are food and energy. And it may not be quite such a problem in America, but in Europe it's going to become very acute this winter. So, I can see huge great problems on the inflation front, which could destabilize the whole of the financial system.

Dennis Tubbergen:

Well, if you're just joining me, I'm chatting today with Mr. Alasdair Mcleod. Alasdair is the head of research at Gold Money. You can read his work at goldmoney.com. I would encourage you to do that. And, Alasdair, you mentioned that these issues will really come to light here this winter in Europe. And you wrote a piece, which is one of the reasons I reached out to you to get you back on the program, if I could. You wrote a piece, title, Winter in Central Europe and for the Dollar, can you just delve into what is going to happen in Europe in your view this winter?

Alasdair Macleod:

Yes. I mean, well, we've just described the winter for the dollar, I think. The problem now we face is that there is a new phase in the special operation as the Russians call it. They're now calling it, if you like, an attempt to attack terrorism, they are specifically avoiding the term war. And what they're doing is they're doing a reverse siege. They're bombing out all the power generation facilities in the Ukraine to make it impossible for the Ukrainians to survive the winter there. So that's going to create, I think a massive refugee problem as this winter sets in. And it's a new phase in the whole of, if you like, the geopolitical struggle between Russia on the one hand and America on the other, and America with its allies. And it's interesting to note that there have been some overtures towards a settlement, try to negotiate some sort of settlement.

And that's something that comes and goes in the headlines, but has it been particularly noticeable in the last few weeks? And I suspect that the both sides will try and move towards some sort of settlement, but in this the Russians I think are in a stronger position than the Western NATO alliance. But as far as Europe is concerned, there's squeezed in the middle. And so, this is their winter, as it were, a very nasty winter because they can see that they're affected by the shortage of energy as well. There's going to be real problems, particularly amongst the poorer elements in the European Union. And on top of that, they're likely to have a refugee problem emanating from Ukraine. So, all told this is not going to be a very pleasant winter for Europe.

Dennis Tubbergen:

And Alasdair, there is talk among the BRICS nations of developing a commodity backed currency to be used in trade to bypass the dollar that that's somewhat related to this. Do you have any updates on that, and how do you see that playing out?

Alasdair Macleod:

Yeah, it's more than BRICS. It's really the Eurasian Economic Union, which is if you like, a mixture of China, Russia, bylaw Russia, and the various stands in the middle of Asia. They are trying to cobble together a separate trade settlement currency between them. The objective being that it should be open to being used by other nations as well who might join in. We've got no further updates on that at all. But all I can say is that I've tried to examine this proposition as much as I can and come to one conclusion, and that is that the only way they can do it really is to have some sort of index currency probably based on gold. Now interestingly, the person who is responsible for the committee taking the decision on this, a guy called Sergey Glazyev is also the man who is behind the new Russian or new Moscow Gold exchange, which has been proposed in the last month or so. So, I think that indicates that his thinking must be going in that same direction. But other than that, Dennis, I really have no further updates at this time.

Dennis Tubbergen:

Well, Alasdair, we have about one minute left in this segment, maybe a minute and a half. Would you like to give our listeners an update for those who may not be familiar with Goldmoney and what they do?

Alasdair Macleod:

Yes, thank you very much. We store precious metals, gold, silver, platinum group metals for people all around the world. And we offer a custodial service, which in other words it remains our customer's property in a number of vaults all around the world. They're all insured, managed by members of the London Bullion Market Association. So, it's about as secure as you can get. And my role in that basically is to try and educate people about the difference between unsound and sound money. And legally this sound money is actually gold, and we need to get sound money back into the system so that people's savings aren't debauched by government action. So that's really our mission in life, and it's a very easy way for people to buy and sell precious metals and to store them.

Dennis Tubbergen:

Well, thank you for that. My guest today is Mr. Alasdair McLeod, head of research at Goldmoney. The website is goldmoney.com. I'll continue my conversation with Alasdair when RLA radio returns. Stay with us.

I'm Dennis Tubbergen, you are listening to RLA Radio. My guest on today's program is Mr. Alasdair McLeod. He is the head of research at Goldmoney. You can learn more about gold money at goldmoney.com and Alasdair's articles are posted there under the Our Research tab. I'd encourage you to check that out as well.

Alasdair, at the end of the last segment, you were talking about this Moscow Gold Exchange that's been proposed. Can you fill the listeners in as to what that is, and what it might mean as far as when a world currency might return to a gold standard or quasi gold standard?

Alasdair Macleod:

Yes, Dennis, certainly. I mean this was something that was announced by Sergey Glazyev who's the same man behind the committee looking at a new trade settlement currency between the Eurasian Economic Union members. I'm assuming that there is a link between the two, but actually what Glazyev said was that this was demanded by the mining and refining industry in Russia, which has been excluded from the LBMA. So I mean I would think is a very good reason and therefore potentially a very good cover for his overall plans when it comes to the new trade settlement currency. It all fits in pretty well with what China is doing as well. And there are links on the gold front between Russia and China already. And I would guess that the standard that they would use wouldn't be the London 400 ounce bars, but I think it would probably be the Chinese 49s one kilo standard. That to my mind is a lot more likely.

And I would also note that a number of Asian interests have already moved over towards the Chinese standard. I was warned quite some time ago, I think back in 2014, that Middle Eastern interests were sending 400-ounce LBMA bars to Swiss refiners to be recast into the new Chinese one kilo 49s standard. And so that was all the way back in 2014, and now we find that Saudi Arabia is intending to join BRICS next year. There is no doubt that this grand plan between China, Russia, Shanghai Cooperation organization, the Eurasian Economic Union, which I've already mentioned, and BRICS, which we've already mentioned as well, all this is coming together into a huge great union which dwarfs the Western Alliance, and the center of all this is gold.

So, in that sense, I would think a physical exchange in Moscow twined perhaps and working with the Shanghai Gold Exchange, which again is a physical exchange, I think is a logical development in that overall geopolitical context. But we have no further news so far as I'm aware other than what I have just stated and the assumptions that I've drawn from it.

Dennis Tubbergen:

Well, Alasdair, before we get onto the next topic, I want to speculate or have you speculate a bit if you would, and that is if Saudi Arabia joins BRICS, does that mean that the petrol dollar's death is now imminent? I mean, is that going to happen next year? Is that going to happen soon?

Alasdair Macleod:

I think in effect he's calling time on the petrol dollar. It's interesting because as we are recording President Xi is visiting Saudi Arabia. Now why is he visiting Saudi Arabia? Well, I think last month he came to an agreement with Qatar, for Qatar to supply China with liquid natural gas for the next 27 years. I think Xi is planning to do a similar deal with Saudi Arabia for oil. So, the answer basically is that these interests, these Saudi interests are moving very firmly towards the Russian and Chinese axis, if I can call it that way, the greater Asian arrangement. And of course, that is going to impact on the petrol dollar. It's going to impact, I think, on the reason that people hold reserve dollars, they could end up reducing their reserves, particularly as this very important, if you like, signal for trade is moving from dollars into the Asian currencies.

And there's a further point which I think is worth making, is that the Saudis have indicated that they are prepared to accept Asian currencies, but I think that they will probably want to say in the stability of those countries the currencies. So, they are likely to have an input, I think, into the new trade settlement currency proposed by Sergey Glazyev as chairman of the committee of the Eurasian Economic Union. So, all in all, I think we answered your question is yes, in time it is likely to reduce demand for the dollar, and I think we can probably call the petrol dollar we're virtually dead now.

Dennis Tubbergen:

Well, let's shift gears a bit, Alasdair. And if you just joining me, I'm chatting today with Mr. Alasdair McLeod. He is the head of research at Goldmoney. The website is goldmoney.com. Alasdair, we talked a bit before we actually started to record this segment about the role of rising interest rates around the world and the effect it may have on derivatives. So, can you maybe give a quick 101 basic explanation of derivatives and then jump into what some of these consequences might look like, and then how some of our listeners might be affected?

Alasdair Macleod:

Yes, certainly. There are two forms of derivatives in the broader sense. You have got the ones we're all aware of, which are regulated futures and options such as on Comex and similar markets elsewhere. And there are the over-the-counter derivatives, which are individually negotiated derivatives, which are far larger than the regulated markets. The regulated markets are roughly, I think $40 or $50 trillion nominal value or notional value, while the OTC markets run as an estimated $600 trillion. Now, these are huge numbers. The only ones that really matter I think are the foreign exchange contracts, which are either forwards or swaps. All these basically involved the dollar, now that they come to around about $80 trillion. Now that's roughly, I suppose it's about 80% of global GDP, which is estimated to be about a $100 trillion. So, this is not an inconsiderable sum. Now the reason these derivative markets have increased is that they've done so against a long-term trend of declining interest rates.

Those declining interest rates basically ended at zero in March 2020 when the Fed cut its rate down to zero and introduced QE at the rate of $120 billion every month. Now that has changed. So, we've got a turn, if you like, in the long-term trend of interest rates, and clearly while in the next, I don't know, sort of three, four, five, six months, it's not clear because we've got a potential recession and how that might affect the Fed's policy. We don't really know at this stage, but I think it's becoming clear that the long-term trend of interest rates is likely to continue to rise. Why? Because currencies are now weakening against commodities inflation in the sense of producer prices, consumer prices, and so on and so forth. Those pressures seem to be not going away. They will continue and probably with further expansion of credit, they will probably continue to increase as well.

So, the long-term transfer interest rates is to rise. Now, the effect on the derivative markets is likely to contract them in exactly the same way that falling rates increase the quantity of derivatives. I would expect rising rates to contract them. Going back to the currency swaps and forwards, these are roughly 80 trillion, as I said before, most of which involve the dollar on one leg. In other words, people have either bought the dollar or sold the dollar for another currency, and that the notional amount is not on bank balance sheets. What they do is they value contracts on a mark to market basis, and that basically means that what's shown on their balance sheets is a fraction of that total. So, we can see that if there is trouble in that market, and bear in mind that the trend of the dollar has changed from increasing its purchasing power relative to other currencies to a decline against those currencies.

If we get trouble in the foreign exchange markets, then the scale of those problems are likely to be very, very severe. I wrote about this at the beginning of last month, and I was interested to note that the Bank of International Settlements produced a paper earlier this week saying exactly the same thing. So, it's not just my imagination. I think this could be a real problem. Of the 600 trillion, the bulk of that are interest rate swaps, and the notional amount doesn't really matter because the notional amount never comes to play. That's just basically a marker, if you like, for the underlying quantities. So, the real problem I think is in foreign exchange contract and also commodities. That's another aspect. And I think that banks are likely to try and reduce their exposure in these areas partly because of Basel 3 regulations, but also, I think because their balance sheets are highly leveraged and they will try and reduce that leave risk as much as possible and as quickly as possible.

Dennis Tubbergen:

So, Alasdair, the time we have left as you were talking, it just occurred to me that this is really a perfect setup for more banking failures and perhaps a repeat of the great financial crisis that we saw maybe 13 years ago or so. Is that valid in your view?

Alasdair Macleod:

Yes, it's entirely valid. And I mean, I just hope that... Well, we've all got to hope that this time a central bank like the Fed won't turn around and say, "Well, we've got to make an example of someone. We'll just let Lehman go." Because the fundamental function of a central bank or one of them is to protect the public from commercial banking failures, and they really can't afford to let any go this time. And having said that, the systemic risks, particularly from foreign banking networks like the Eurozone, which is very highly leveraged, also Japan is very highly leveraged. These risks are very, very substantial. And with contracting bank credit, they merely get heightened. So yeah, this really is, I think it's got the makings of one of these periodic banking, cyclical banking crises. They happen roughly every 10 years. So this cycle has been long in the tooth and it's overdue for us to have. Well, you call it kindly a correction, but I think probably a crash is more, even though it's a better description.

Dennis Tubbergen:

Alasdair, just in 30 seconds or so, what would you advise listeners to do? Obviously, are we going to go back to our tangible assets where you need to be, I mean, gold and silver seems like the only asset that probably will not be affected here.

Alasdair Macleod:

Well, yeah, I mean, I don't give investment advice, but my personal view, and this is based on my studies, is you've got to get at least some of your life out of the fiat currency system. I hope I'm wrong about what we have been talking about, but if you think there's some truth in what I'm saying, then I think to get out of the fiat currencies by having some gold and silver has got to be... And it's physical, by the way, in your possession or stored with someone like Goldmoney, that I think is probably the safest policy that you can possibly enter into.

Dennis Tubbergen:

Well, that's a good place to leave it. The clock says we're out of time. My guest today has been Mr. Alasdair McLeod. He is the head of research at Goldmoney. If you'd like to read his work, you can go to goldmoney.com, and you can learn more about the work of Goldmoney there as well. Alasdair, thank you for being so generous with your time. I know it is in demand, and I appreciate you being here. I know the listeners do as well, and we'd love to have you back down the road for an update. Thank you very much.

Alasdair Macleod:

Thank you, Dennis. And I'd love to be back at some time.

Dennis Tubbergen:

We will return after these words.