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A Single Global Currency

It was both a privilege and a pleasure to attend this past Friday the first meeting of the Single Global Currency Assn., http://www.theunionleader.com/articles_showa.html?article=40597 The meeting was the idea of Morrison Bonpasse, founder of the SGCA, which held their conference at the beautiful Mount Washington Hotel & Resort in Bretton Woods, New Hampshire.

That venue was purposefully chosen because this year marks the sixtieth anniversary of what is now called the Bretton Woods Agreement. Signed during World War II by the Allied powers, the agreement established the basic structure of the international monetary system for the post-war world. Though it did not envision a single global currency, the agreement made the US dollar as the world's reserve currency, which has since become the dominant currency in international finance.

I agree with former Federal Reserve chairman Paul Volcker's statement that "a global economy requires a global currency." However, that broad statement of principle leaves open the question of how it is to be achieved, which is why I attended the SGCA conference. I have strong, clear views on the issue of money and currency and wanted to ensure that my point of view was represented. And what is my point of view?

Basically, I agree with the thinking of Ludwig von Mises who noted that currency is too important a component of society for it to be put into the hands of government for management. Instead, currency – like any other good or service – should be a product of the free-market.

For example, central bankers do not have any bottom line accountability. They don't care whether or not they make a profit. Their actions are instead influenced by and subject to government intervention and manipulation, which undermines the usefulness of any currency. To be most effective in commerce, currency should be a neutral tool in commerce, but political decisions erode and can even completely destroy that neutrality and the unbiased nature that a currency should have.

Free-market currency on the other hand is fundamentally different. It is a product of the free-market, which itself is the result of voluntary interaction by individuals seeking to improve their position. Free-market currency is a product of the market process. If a company creates a currency that people find useful, they will use it and pay to use it. If the currency is sufficiently accepted, the company will make a profit and stay in business.

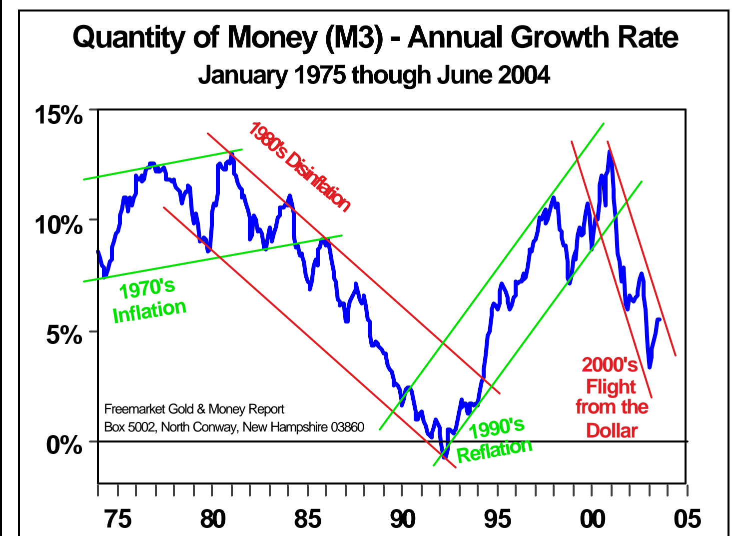
This bottom-line accountability is absent from central banking. Central bankers stay 'in business' regardless of how well or poorly they manage their currency. And experience shows central bankers more often than not manage the currency poorly. Consequently, I do not support the idea of a single global currency managed by a global central bank, nor any fiat currency that is forced to circulate – regardless of the quality of that currency – because of government mandate.

If currencies are allowed to compete on their own merits, a single (or not more than a few) global currency will emerge in time. It will be the reverse of Gresham's Law, where bad currency drives out the good currency when the two are made to circulate as equivalent because of government mandate. Instead, without the government intervention, good currency will drive out bad, which will be a result regardless whether that currency intends to circulate just nationally or globally.

Readers will probably recognize that a lot of this thinking has gone into GoldMoney, http://goldmoney.com/ With GoldMoney we are delivering a currency that competes on its own merits, and circulates because it is useful, not because of government mandate or legal tender laws. It was this message that I delivered to the SGCA conference, and I am hopeful that this thinking about free-market currency will help shape the basic principles upon which the SGCA is being founded.

I encourage you to learn more about the SGCA and to visit its website, http://www.singleglobalcurrency.org. Also, if you consider the objective of a single global currency to be worthwhile, the SGCA would welcome your support and donation. They accept most major national currencies as well as GoldMoney – their Holding name is Single Global Currency, and their Holding number is 51-41-17-A. ¤

DOLLAR SUPPLY Over the past six months, the Federal Reserve and the banks have been vigorously pumping up the money supply. We can see this growth on the chart below. The near straight-up trend since December is one of the sharpest ever recorded over such a short period of time.



What's going on? It seems to me that the Federal Reserve is encouraging this money growth for either of two reasons, and possibly both. First, it believes that the economy is not doing as well as it would like. So it is trying to nurse the economy along by allowing more dollars to be added to it in the hope that these dollars will bring growth to the economy. Second, the Fed may be trying to liquefy the economy in anticipation of a looming crisis, such as one that would no doubt occur from the collapse of a major market player. For example, when Long Term Capital

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Management collapsed in 1998, the Fed opened the spigots to make sure that newly created dollars were flowing to abundance.

I don't have the answer to the Fed's actions at this time, but I comment more about this matter on page 4. ¤

THE STOCK MARKET The rally in the stock market seems to be coming to an end. Stocks look vulnerable here, as can be seen on the accompanying weekly chart of the S&P 500. Stocks look ready to again head lower within the broad downtrend channel shown on the chart immediately to the right.

The second chart is even more important. Since the 1999 low in gold, investors have been better off by holding gold in preference to stocks (excluding the gold mining stocks of course). It has been my contention that this result will continue for years. If we compare the past year's results of these two charts, we can see that the S&P 500 has rallied in dollar terms, but only gone sideways in terms of goldgrams. In other words, gold has been doing relatively well, even as the stock market has been climbing.

Investors remain on the sidelines with their purchasing power safely parked in goldgrams. Traders are on the sidelines as well, but I think they should now sell short the SPY (today's close for record keeping). Stop out this trade if the SPY closes more than 5% above your short sale price or above $115.00, whichever level is lower. I do not recommend shorting the DIA or QQQ at the moment. I would like to see some more downside confirmation in the market's action before taking that step. ¤

GOLD STOCKS The gold mining stocks are bouncing back as gold climbs higher. For example, the XAU is up 13.7% since June 14th, the date of the last letter.

I've been advising that we should keep accumulating the gold mining stocks on my recommended list. The important point I've noted before is worth repeating – gold stocks are undervalued because gold itself it undervalued. This reality is the fundamental driving factor why gold stocks should continue to be bought. ¤

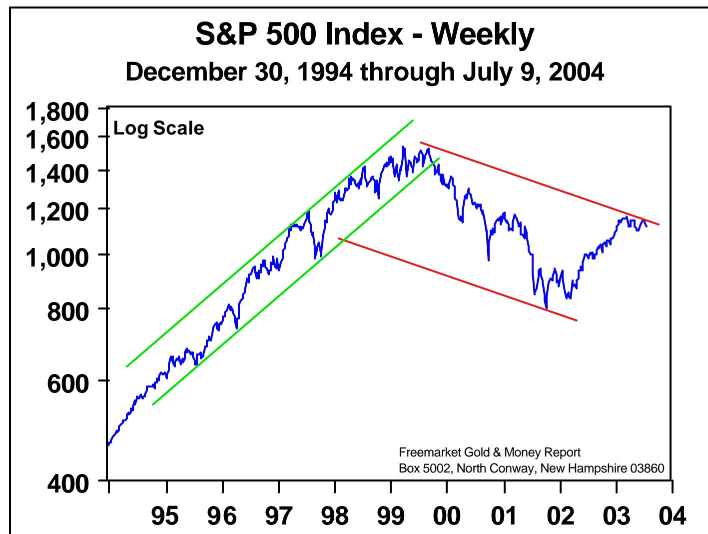
INTEREST RATES In the past, the huge debt of the federal government was often explained away with the expression that the debt doesn't matter because 'we owe it to ourselves', as if that hollow slogan provided sufficient justification for the government to incur debt. Well, even that non-excuse no longer applies because for the first time in history, foreign holders now own more federal government debt than Americans.

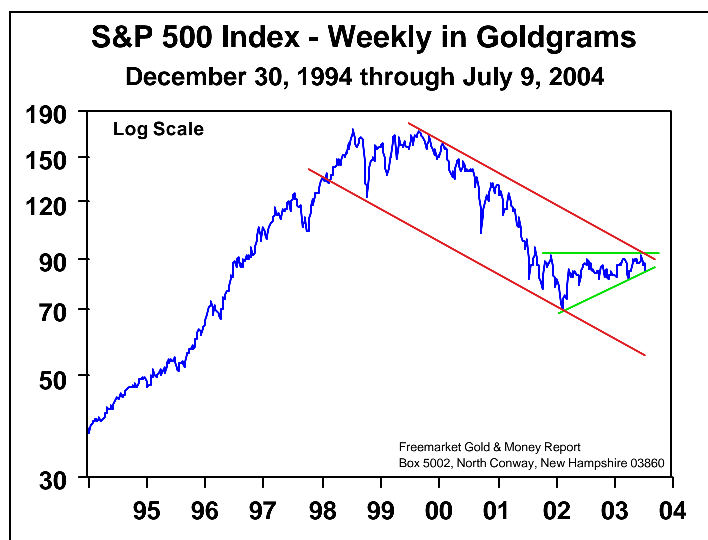
Federal Reserve figures reveal that $1,653 billion, or 50.6% of US government debt instruments, were held by foreign holders at the end of the first quarter. It is just one of the new records being set daily as the US debt bubble continues to inflate.

Interestingly, of the $170 billion increase in debt held by foreigners in the first quarter, it is estimated that $96 billion was purchased by central banks. This growing trend of central bank purchases explains why I have not sold short T-bonds and T-notes, even though they are in bear markets.

I have repeatedly stated that the prices of federal debt instruments have remained relatively stable only because US government debt is being bought in increasing quantities by foreign central banks. Further, a weak dollar means that these purchases will continue, and as long as they do, T-bond and T-note prices will not fall to their natural level.

Consequently, continue to sit on the sidelines as far as T-bonds and T-notes are concerned because central banks will on balance continue to accumulate dollars to prevent their currencies from appreciating against the dollar. This reality of course is very bullish for gold, because central banks create new currency to make these purchases, which debases these currencies almost as rapidly as the dollar is being debased. But central banks inflate





away their fiat currencies rather than face the consequences of rapidly rising interest rates if central bank buying of US debt instruments were to slow.

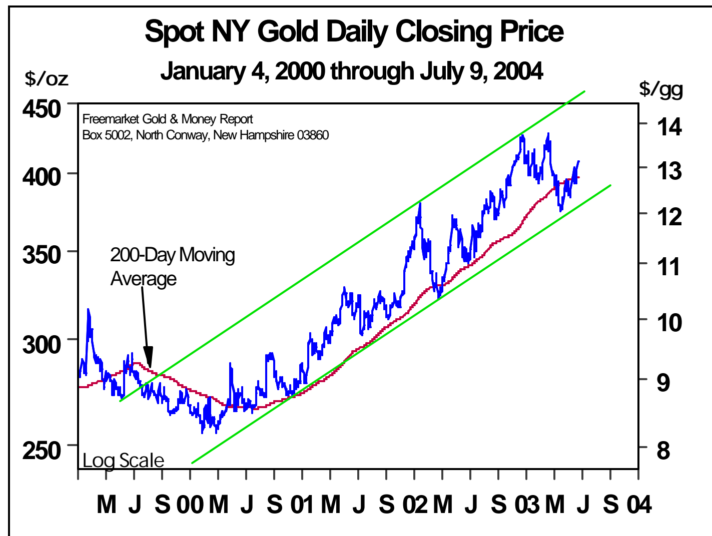
Interestingly, the gross federal debt declined $14 billion this past week. It appears that the feds are trying to avoid exceeding the current federal debt ceiling, which is only $124 billion away. So this week's decline in the debt is probably the result of 'smoke & mirrors'. Various questionable techniques have been used in the past to avoid the ceiling. It appears that they are now again being put into place. ¤

SILVER TRADING Over the years I have from time to time mentioned my friend Franklin Sanders, a coin dealer who lives in Tennessee and editor of *The Moneychanger*. Franklin has just finished writing an excellent 90-page 'how-to' manual about trading physical silver, but also includes his current thinking on the outlook for silver. Additionally, it is filled with much useful information and interesting facts and charts.

This manual's cover price is $199.00, but you can purchase it for just $49.00 plus shipping. To get this discount, you only need to mention that you heard about this Silver Trading Manual from me or FGMR.

Order the Silver Trading Manual using your Visa or Mastercard by calling (888) 218-9226 or (931) 766-6066. ¤

NEXT MAILING The next issue of FGMR is scheduled for mailing on July 26th. ¤



RECOMMENDATIONS (Basis spot prices and assumes that trading is non-leveraged).

(1) Trading Portfolio: (For short-term traders).

GOLD – Traders are long one position from $385.60 on May 24th. On June 18th they added one position at $395.10. Traders also bought gold at $403.10 on June 24th. Stop out these trades on the first New York close below $392.

Regardless what happens to the above trades, traders should buy one position on the first New York close below $398. Stop out this trade on the first New York close below $392.

Also, buy one trading position on the first New York close above $412. Risk $8 on this trade as a stop-out point, basis closing New York prices.

SILVER – On June 14th traders bought one position at $5.655. They then added by buying a second position on June 17th at $5.922. Stop out these two positions on the first New York close below $5.96.

Another position bought on June 24th at $6.173 was stopped out two days later at $5.897 for a 27.6¢ loss.

On July 8th traders bought one position at $6.42. Stop out this trade on the first close below $6.12.

I recommend that traders buy silver on the first New York close below $6.30. Risk 15¢ on this trade, basis the closing New York price.

CURRENT MARKET SITUATION Gold continues to act well. And although readers know that I have been bullish about gold's prospects, gold in fact is performing even better than I expected. I already mentioned this phenomenon of better than expected strength in the last letter.

I said that even though gold did not manage to hold above over-head resistance around $394 on its first stab, "*by taking that shot at $394 as early as it did after its recent setback, gold in my view was actually displaying inherent strength, which bodes well for the future*." We've now seen over the past few weeks what I was only sensing back when I wrote those words. Gold has shown impressive strength, first by holding well above major long-term support in the $380's, and then by moving back above its 200-day moving average as well as the important $400 level. So is gold now ready to soar?

Well, anything is possible. And the underlying fundamental factors that have been so bullish for gold are day-by-day becoming even more bullish, so gold could clear $430 at any time. To emphasize this point, gold could clear $430 in the blink of an eye. We have to be prepared for that possibility. But I still think it is too early to get too excited. My best guess is that gold needs to test support under $400 one or two more times, over the next month or two.

Take a close look at the accompanying chart. The long-term picture for gold remains clearly bullish. Not only is gold trading well within its uptrend channel, it is also above its 200-day moving average. So gold is clearly in a long-term uptrend and that is obviously the most important consideration. But the key question remains as to whether gold now has enough support underneath it to launch an attack on that double top you can see on the chart that was formed early this year.

In the 'for what it's worth' category, I think gold needs to build more support. Consequently, I have not been expecting gold to begin its next big move until September, and that all the action from its reaction low until then will prove to be base building. We now have a couple of months of that base building, but I think more is needed. (cont'd on page 4)

GOLD/SILVER RATIO – On May 10th traders sold the gold/silver ratio at 65.7 (they bought silver and sold an equal dollar amount of gold). Unwind this trade if the ratio closes above 68.4.

(2) Strategic Portfolio: (For long-term investors).

Since I began writing this newsletter in 1987, I have been recommending the on-going accumulation of gold bullion. During much of this period (and most lately since Letter No. 272-10 was published October 20th, 2000), I have been recommending the accumulation of mining stocks. As long as gold is below $500, continue accumulating both the metal and the stocks. However, once gold goes over $500, then it is time to stand aside and happily watch the price appreciation of assets that were carefully and steadily accumulated when they were undervalued.

(3) Options: (For experienced traders; basis COMEX).

In the last letter I recommended that "we should again be looking to write puts", but my entry level on gold was not hit.

I think it is too early to be aggressive with options here, so my thinking is to sell puts if gold pulls back into support. My recommendation is to sell the Oct 390 put on gold's first New York close below $398. Buy back this put if gold subsequently closes in NY below $392.

Remember, option recommendations are high-risk trades and are therefore not for everyone. ¤

So for the fourth letter in a row, I am now giving basically the same advice. Do not expect much upside price action from gold for a while. It still needs time to re-build support. But note also that my advice is different in the sense that we must recognize that we are now several weeks into the base building process. Thus, with each passing day we are getting closer to that moment when gold takes off to the upside and does not look back.

Consequently, our job is now getting tougher. First, we have to look to build our trading position on pullbacks into support if they occur. But also, we have to be prepared to buy on strength if gold starts moving higher from here, and all the while we need to try avoid being whipsawed by volatility.

The objective is to build a meaningful trading position while gold is base-building, and then hold this position as gold climbs in a new up-move on a break above $430, which I expect will happen by September. And once gold breaks above $430, $500 is just a chip-shot away. So $500 is a reasonable target to be achieved by the first quarter of 2005, if not before.

Silver is showing even more strength than gold. Some interesting developments can be seen on the page 3 chart.

First, silver is holding within the wide uptrend channel shown of the chart. When I first drew this chart a couple of months ago, it was highly uncertain whether this pattern was valid. It was in other words very speculative of me to suggest that uptrend pattern when I did. Nevertheless, that speculation has paid off because it has provided an accurate indication of silver's overall technical picture.

Another important development is the pennant formed by silver, partially with the bottom line of the uptrend channel. Note that silver has broken out of the pennant to the upside.

Lastly, silver is above its 200-day moving average. What's more, that average is continuing to climb higher.

In summary, the picture for silver remains bullish. But as is the case with gold, I do not expect silver to aim just yet for the $8+ area it reached earlier this year. Silver needs to do more backing and filling. Nevertheless, I expect that silver will be back above $8 when gold climbs above $430. Then when gold touches $500, silver will be at least $10, which puts their ratio at 50.

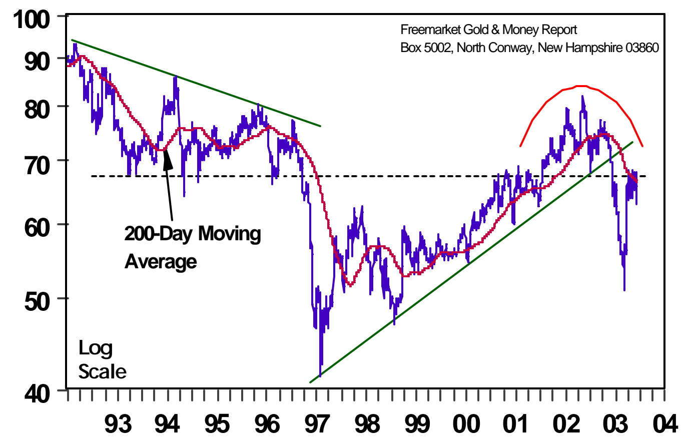
However, as we can see from the ratio chart on this page, I may be too conservative in my expectations for silver. This chart shows that the ratio could easily fall once again to 40. With gold at $500, a 40 ratio puts silver at $12.50.

The bottom line is that the precious metals remain in a major bull market. What's more, their correction over the past few months is ending. We should therefore continue to expect much higher prices metal prices later this year. ¤

POTENTIAL FLASHPOINTS As I noted in the last letter: "*There are a large number of potential flashpoints that could send the metals soaring*." Add to that list a growing banking crisis in Russia. The knock-on effect from this new crisis should probably start appearing in the next several weeks. You may recall that when Russia had a similar crisis in the summer of 1998, it took until October of that year before Long Term Capital Management collapsed.

While on the subject of flashpoints, I have been repeatedly warning about Fannie Mae and Freddie Mac. I mentioned them again in the last letter, noting "*the continuing uncertainty about the financial position of Fannie Mae and Freddie Mac and their derivative positions (which uncertainty by the way will only grow if the Federal Reserve starts raising interest rates)*."

Well, the Fed did raise interest rates a token 0.25%. That jump was so little and so late in the cycle that it won't do anything to stop the resurgence in inflation. But it will have a



knock-on effect, as will other jumps in rate to come. I mention this because of an article that appeared this week in *Forbes*, http://www.forbes.com/business/2004/07/06/cz_rl_0706soapbox.html. It was written by Richard Lehrman.

I highly recommend that you read this article, as Mr. Lehrman carefully points out the risks in Freddie Mac, which in my view also apply to Fannie Mae. To highlight a couple of points, he notes "*The revised* [financial statements] *show that Freddie broke even for the second half of 2003, after a profitable first half. Losses from its derivatives trading--the source of the accounting problems and of some $4.3 billion in losses in the second half of 2003--were the cause of the poor second-half showing. To refresh your memory, interest rates fell in the first half of 2003, and they rose in the second half. Perhaps you need not be reminded where they've gone since April of this year.*"

Mr. Lehrman also observes astutely: "*Reporting bad news still does not come easily at Freddie, so we need to look to other sources of information. First, we hear that banks are reporting they expect to benefit from interest rate rises, contrary to past experience in rising rate environments. Since they are big in the derivatives markets, where Freddie is one of the biggest players, it may well be that their optimism is because they are the counterparties to Freddie's derivatives contracts*." To put it another way, derivative contracts are a zero sum game. For every winner, there is a loser, and if banks say they are the winners, Freddie and Fannie appear ready to take on that role of loser.

Lehrman goes on to say: "*Also, look to Fannie Mae's reporting for the first quarter of 2004. It reported losses of $1 billion on derivatives, and this was before rates started rising in April. Since both companies have about $1.3 trillion in such contracts, Fannie's loss may be a fair estimate of Freddie's loss.*"

Lastly, to make his message abundantly clear, Lehrman concludes "*the concern has always been that rising rates could cause Freddie to implode, much like the Long Term Capital Management hedge fund or the Orange County investment fund. Only, this time, the fallout could cause a systemwide financial panic*." I think an implosion of Freddie and Fannie are inevitable, just like it was for John Law's infamous Mississippi Company. ¤

CURRENCY COMMENTS We hold goldgrams acquired on March 23rd, 2001 as our Core Currency Position. Continue to hold the bulk of your liquidity in goldgrams.

I suggested in the last letter that "*the dollar's bear market rally appears to be ending*." It now seems clear that it has. Continue to watch for my analyses of the dollar and charts of the US Dollar Index posted at www.goldmoney.com ¤