The Argument for Returning to the Gold Standard: The Lessons of Contemporary History

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Benn Steil and Manuel Hinds emphasize a remarkable truth in their book, *Money, Markets, and Sovereignty* (2009). This is that the last forty years is the only notable span of time in all of human history when some sort of metallic money standard has not been predominant in some important part of the world. Whatever the prior history of fiat money, before 1971, mainly gold, but other metals such as silver and copper played central roles in so many major economies that the phenomenon rises to an unremitting narrative of the human species.[1]

Four decades removed from this sine qua non of the past—a past which fully included the centuries of the industrial revolution—we can begin to assess the effects of our own *novus ordo seculorum*. There have been four decades of the fiat money era: the 1970s, the 1980s, the 1990s, and the long 2000s. Two of these decades were flatly unacceptable in terms of economic performance. The stagflationary 1970s represented one of the worst eras of the American, if not the world economy outside the Great Depression-laden 1930s. In turn, the dozen years since 2000 have by consensus come in as an extended lost decade that threatens to undermine bedrock confidence in the American dream.

However, the middle decades, the 1980s and the 1990s, and more precisely the period 1982-2000, saw the kind of excellent growth, employment opportunities, entrepreneurial panache, and technological change that the industrial revolution of yore had gotten the Western nations used to in the first place as the regular course of things.

There is a control across these decades: the price of gold. In the 1970s and the 2000s, this price moved like a rocket, increasing 23-fold (no misprint), from $35 an ounce to levels over $800. And from 2000 to 2012, the increase has been six-fold (and rising), from about $300 to over $1700. From 1982 to 2000, in contrast, the price of gold was low and stable at roughly $350 an ounce. The correlation is this: manic and increasing gold—severe economic underperformance; gold largely forgotten about as an investment class and consistently in the price doldrums—economic renaissance.[2]

It would seem that the experiment in fiat money since 1971 only verified what was widely known in the vast history before. This is that well-run commodity-money standards, in particular that of gold, in which currency issuers themselves exchange their issues in gold at a fixed price, have within them the resources to deliver whopping economic results. And further, that fiat money systems—unless they ape the gold standard itself—have an unusual propensity to direct monetary resources away from real purposes.

The major argument for returning to the gold standard now is that it has succeeded in the past, and done so splendidly. Another argument is that it has not failed in the past, in that virtually all "panics," "depressions," and such of the gold-standard eras correlate to attempts to dilute or otherwise finesse the gold-standard system. Yet another argument, all too pertinent to us today, is that the fiat money era is capable of bringing the economy to a state of such poor performance and demoralization that people are apt to forget the heights that economies since the industrial revolution are apt to scale and conquer. If we do not return to gold, our very economic horizons stand to be narrowed.

This paper shall make some remarks about the unitary history of the gold standard in American economic history, a history of unprecedented growth in the real sector in the context of stable if lightly declining prices. It shall also point out that the blips in the grand history of gold in this country must not count as any argument against the reinstatement of gold today, in that these invariably represented ill-advised attempts to buck the discipline of gold.

But the central purpose of this paper is to outline two things, both concerning the economic history of this country since 1945. The first is the remarkable correlation between stable gold and the great, fabled modern runs of prosperity. The second is the manifest necessity to seize the opportunity of the low and stable gold/extended prosperity connection and, during such events, make a *formal* conversion to a gold standard.

The paper shall be at pains to observe that the great runs of 1945-1969 and 1982-2000 provided exceptionally propitious circumstances for an official and comprehensive return to gold. If only these conditions could be replicated in our own day, this nation would regain position to take advantage of the greatest missed opportunity in economic affairs in our recent history.

When gold is low and stable in price, in an inconvertible system (such as since 1971), what is going on is that economic agents are delivering a clear, two-fold message: first, that opportunities in the real sector are excellent; and second, that the monetary authority is trustworthy. On both counts, gold does not attract purchasers. Therefore, this is precisely the occasion when a gold standard is easily implemented, in that the currency issuer (the government) could formalize the price of gold, which informally is constant and reflective of lack of interest in the first place. The benefit that stands to come from such an action is that the excellent real-sector conditions making possible an easy return to gold would persist into the future, on account of the official stability of gold.

It is simply a *trivial matter* to establish a gold standard when gold is low and stable in price. For example, had the United States gone back on gold in the Ronald Reagan/Bill Clinton days—say at the prevailing $350 an ounce—it is highly likely that the results would have been no less than as follows: the domestic and international monetary systems would have experienced no disturbance; and the great boom of the 1980s and 1990s would have been extended far into the future, into the 2000s and our own 2010s, with no lost decade and no Great Recession such as we have had to deal with in fact.

Thus this paper shall strive to show that of all the reforms that bore along the boom after World War II, and that began and sustained the “Great Moderation” (as it is known) in 1982, which is primarily to say the restriction of taxation and government spending (or rather the appreciable limitation of the state)—one further reform should have been added in both cases, and must be added should we have the chance again, with so much in terms of prosperity, opportunity, and the continuance of the tradition of the industrial revolution in the balance. This is monetary reform in the clear direction of convertibility in gold.

“Can’t Stand Prosperity”

There is a saying in the sport of golf, “You can’t stand prosperity.” People use it on the course when they follow up a good shot or hole with a bad shot or spate of play. What are golfers doing ruining a good thing, instead of keeping a good thing going, is the gist of the aphorism.

This question might well be asked of the United States with respect to several junctures in its grand economic history when it fooled around with getting rid of the gold standard. Perhaps none of these examples is so pronounced as what happened at the end of the great post-World War II run in the early 1970s.

The single most famous and cherished era of all of American economic history, in the eyes of the present generation, remains that of “postwar prosperity.” This was the splendid twenty-five years or so after World War II ended in 1945 when growth was strong year after year, employment was not only steady and secure but increasingly remunerative, new businesses (from fast food to the awe-inspiring enterprises of Silicon Valley) emerged to change the American landscape and sense of the possible, and American economic leadership inspired many places around the globe to emulation. From Paul Krugman on the left to Tom Wolfe on the right, and to numerous observers of all stripes, the late 1940s, the 1950s, and the 1960s stand as the quintessential era of the American dream.

There are quibbles to be made with holding up postwar prosperity as great shakes—there were runs in the 19th century, for example the post-Civil War quarter century, that really should be more famous—but let us take the basic point, the national consensus: postwar prosperity was a very good thing.

The exchange-rate order of this era is one of the great buried facts of American economic history. The United States was on a (modified) gold standard the whole while. The simple association that we are prepared to make, therefore, is between postwar prosperity and the gold standard.

Postwar prosperity was co-extensive with what is called the “Bretton Woods” era of international monetary cooperation, Bretton Woods being a conference center in New Hampshire where the principles of this cooperation were set forth in 1944. Under the Bretton Woods system, each participating country (and such countries came to include virtually all of the economically modernized ones) maintained a fixed rate of exchange to the dollar, while the dollar remained convertible to gold to the respective foreign monetary authorities.

Thus were two essential characteristics of the gold standard embedded in the Bretton Woods system. There were *fixed exchange rates* among currencies. A fix to the dollar on the part of foreign currencies meant that de facto all member currencies were fixed to each other. And currencies could be *exchanged for gold* officially, directly in the case of dollars, and indirectly in the case of other currencies, where they first had to be used to purchase dollars themselves convertible to gold. The system departed from a robust gold standard in several ways: not every currency was directly convertible to gold; not all holders of currency, but only monetary authorities, had the standing to ask for gold conversions; the fixed rates could be changed if the authorities agreed to it; and a bureaucratic institution (the International Monetary Fund) attended the whole system to bail out currency issuers not maintaining proper discipline.

At any rate, very important elements of a good gold standard were there, and this was the monetary system that coincided with postwar prosperity. Furthermore, this postwar prosperity was not only a phenomenon occurring in the United States. Germany and Japan experienced growth rates into the early 1960s at 8-10% per annum. France's growth rate was some 6% a year over the same span, with Italy not far behind. Each of these countries had currencies that were notable in their adherence to the fixed-exchange rate discipline. Indeed, the country that most tried to buck the Bretton Woods system, Great Britain (by means of striving not to fix the pound sterling to the dollar, but to gold directly at a manifestly low price), saw the lowest growth rates of any nation that was its peer. Adherence to the approximation of the gold standard that was Bretton Woods correlated directly to the extent of a nation's participation in postwar prosperity.[3]

It remains one of the singular tragedies of modern world economic history that the Bretton Woods system did not come to its final logical maturity. What should have happened as Bretton Woods aged, and as postwar prosperity became an international fixture, is that each successful country should have consistently used a portion of its healthy savings built up during the prosperity to request allotments of gold from the United States, ultimately leave the system, and then establish its currency as directly fixed in gold. The system was primed to do this globally—to effect a return to the classical gold standard—yet this final result never came.

In 1945, as World War II ended, the United States had something like 75% of world monetary gold in its possession. It would have been difficult, if not impossible, in this circumstance, to have countries fix independently to gold, in that the U.S. had virtually all the gold. Thus was Bretton Woods not merely an approximation of the central functions of the gold standard in the context of a one-sided international distribution of gold, but a very good means for re-establishing a comprehensive international gold standard at some point in the relatively near future.[4]

This transition did not happen after postwar prosperity got going mainly for one reason: the United States did not see to it that it would happen. The problem was intellectual. The United States did not recognize the opportunity with clarity, even as it had basically designed Bretton Woods; nor did it divorce itself sufficiently from Keynesian temptations that would make this transition impracticable.

In the 1950s and 1960s, foreign dollar-to-gold conversion requests came on account of two distinct motivations. On the one hand, flourishing countries such as Japan and Germany were seeking to build up gold reserves for reasons such as described above. But on the other hand, countries (above all France) were apt to make conversion requests for the dollar into gold out of the fear that the United States might devalue gold (i.e., raise its official price above the standing $35 per ounce mark). The point, if only the United States could grasp it, was to ensure that gold requests of the first sort happened, and that those of the second sort were made unnecessary.

The easiest way for the U.S. to make sure that countries did not fear for a dollar devaluation was to make the private investment environment in the U.S. a highly enticing one. Given good economic growth in the United States, foreign demand for gold would drop, in that the most remunerative use of dollars would be towards real investment. If there were solid investment prospects in the United States, the demand for gold would revert exclusively to the slow build-up of monetary reserves; hedging the dollar would be superfluous, indeed unwise, if the United States were experiencing an inflation-free boom.

This is precisely the lesson the United States apparently absorbed in the early 1960s, as the John F. Kennedy and early Lyndon B. Johnson presidential administrations pursued policy such that the dollar strengthened (as the Federal Reserve raised interest rates), and as cuts at the marginal rate of the income tax ensured greater real returns from dollar-denominated investments. The young economist Robert A. Mundell who outlined this strong-dollar, tax-cut policy mix at the time (as an I.M.F. employee) would see his work honored with a Nobel Prize in 1999.[5]

The great 1960s boom touched off by this policy mix came in at the heady level 5% per year, 1961-69. Clearly this was a time for the most narrow claims on U.S. gold, i.e. only for the buildup of national gold reserves on the part of successful countries. The boom made it a losing proposition to exchange dollars for gold otherwise: the action with respect to returns was in the real sector. Presumably, the United States could have kept the good thing going by continually making devaluation hedges unnecessary. Further tax cuts and Fed vigilance about overprinting (not to mention deregulation) would have done the job.[6]

Had the United States shown such leadership, and kept the real sector cruising, it is perfectly reasonable to hold that by, say, 1980, not only would the 1970s have followed up the 1960s as a uniquely prosperous decade globally, but the world would have been in a position, in 1980, to have every major currency fixed in gold on the basis of proportionate national gold stocks.

Needless to say this did not happen. But that it could and should have happened must be kept in mind in our present-day considerations about finally returning to gold once again.

The United States began running considerable budget deficits after 1965, implying that the Federal Reserve would print dollars to cover them, jeopardizing the U.S. gold stock and the orderly distribution of that gold to the growing countries participating in Bretton Woods. Then in the recession of 1969-71, the United States explicitly reversed its strong-dollar, tax-cut policy mix in favor of dollar ease, inflation, and effective (and statutory) tax increases.

Thus on two major counts foreigners now wanted gold in scads, neither reason being the foundational one of wanting to build up reserves for an independent gold-backed currency. 1969-71, foreigners wanted gold because the prospect of dollar devaluation jumped markedly with consumer price inflation now running at 6% per year; and because the dollar-area investment environment was less remunerative on account of the tax increases.[7]

It soon became apparent to American leaders that foreign monetary authorities would make a tremendous run on the official U.S. gold stock (and even though these authorities had basically pledged not to do such a thing). At last in August 1971, the United States once and apparently for all ended convertibility of the dollar in gold. For two more years, the fixed-exchange rate system (without the dollar anchored in gold) persisted at the behest of the United States. In 1973, all major countries delinked from the dollar, and the modern regime of floating exchange rates began.

This was also precisely when the great stagflation of the 1970s got up on its feet. The recession of 1969-71 had seen a 50% increase in the unemployment rate, from 4% to 6% (somehow in the context of a ravenous military draft), with inflation also coming in at 6%, five points higher than in 1965, along with a "double dip" in GDP contraction, such that the initial recovery gave way to a negative quarter of growth before sustained recovery came. From 1973 to 1975, all these conditions were magnified for the worse. Unemployment again made a 50% jump, from 6% to 9%, inflation totaled 25% over two some years, and there was a double-dip encompassing five down quarters of GDP change—a feat not replicated until our own Great Recession.[8]

Gold, for its part, quickly went to $175 in the private markets. Thus did the great modern pattern establish its regularity. Low and stable gold, broad prosperity, at home and abroad. High and gyrating gold, severe domestic economic distress and the elimination of a clear basis for the international monetary system.

The era of "stagflation" (a term brought into use in 1974 to capture the apparent contradiction of simultaneous GDP stagnation with price inflation) lasted all the way through the early 1980s. 1966-1982, the price level tripled; the Dow Jones Industrial Average lost 75% in real terms; and essentially three double-dip recessions occurred, 1969-71; 1973-75, and 1980-82. The worst of it occurred in the early 1980s, when in 1980 (a recession year) inflation hit the yearly rate of 14% and the prime rate of interest 22%, these unbelievable statistics only giving way to unemployment reaching for 11% in two years' time. Gold hit $800 an ounce in 1980, only slightly outpacing the 14-fold increase in the price of crude oil since 1971.[9]

On account of these alternatively bizarre and brutal numbers, the stagflation era takes its place as the second-worst extended run of American economic performance of the entire Constitutional era—exceeded only by the Great Depression of the 1930s itself. During this episode, gold had no official role in the monetary policy of the United States, and by extension the international monetary system, and was moreover was not even in abeyance—for the first time in ages.

Reversion to status quo ante

The great turnaround began in 1982, the base year from which both good growth and approximate price stability would proceed apace for the next quarter century. As James G. Rickards is keen to point out in his recent book *Currency Wars*, from 1983 to 1985, the United States achieved 16.6 percent collective real growth, a mark not reached since. But moderate growth thereafter did indeed come. The run from the trough of 1982 through the peak of 2007 was 3.3% per year, the same number that prevailed in the complete run of postwar prosperity, 1945-73.[10]

Inflation, which was running on average at 9% in the 1970s and early 1980s, dropped suddenly by two-thirds to a 3% yearly average in the early phase of this "Great Moderation," with that level holding the whole while. Unemployment fell, if more cautiously, to 5% by the late 1980s, to structural levels below 4% in the late 1990s, to basically below 6% through 2007.

It is difficult to distinguish, on the basis of these notable metrics, any difference between the quality of the economic performance of the nation in the eras of postwar prosperity and the Great Moderation. Likewise, and most intriguingly, it is difficult to distinguish any material difference in the behavior of the price of gold over the two eras.

In the quarter century after 1945, the United States guaranteed a $35 price of gold, and in private markets this essentially was the price, with small and highly occasional periods of stress where the London mark went up to $40, making for incredibly lucrative arbitrage opportunities. It must be kept in mind that there was no domestic market for gold in the United States this whole while (by law).

In the quarter century of the Great Moderation, gold began on a great tumble downward, from the huge 1980s levels discussed above to the $350 level in 1982. For the next twenty years, gold basically averaged $350 per ounce, with occasional forays in the high $400-range and dips slightly below $300. In this period, though the United States was no longer guaranteeing sales of gold to foreign monetary authorities seeking to redeem dollars, there was a domestic gold market (an active one) on account of the U.S. permitting the existence of that market in 1974.

Hence a correlation: 3.3% yearly real growth for a famously halcyon generation (postwar prosperity), with minimal trade-offs in terms of inflation and unemployment, and gold stable at $35 an ounce; and 3.3% yearly growth over a follow-up generation (the Great Moderation), with much reduced trade-offs in terms of inflation and unemployment, and gold stable at "ten times 35" (as *Wall Street Journal* editor Robert L. Bartley would put it in the thick of this run), putting to bed a long interregnum of substantial economic underperformance and the gold price in the stratosphere.[11]

The lesson of contemporary history, of 1945-2007, came to be inescapable with every passing year of the Great Moderation. A low and stable price of gold is the necessary correlate of the kind of economic performance that by rights is characteristic of the world's leading nation.

It is no mystery what attended the rise and the endurance of the Great Moderation. It was a return and an extended commitment to the fiscal-monetary policy mix most perfected in postwar prosperity during the JFK and the early LBJ years. This was strong-dollar monetary policy in conjunction with a retreat of the fiscal in favor of the real sector.

Federal Reserve monetary policy after 1982 probably for some time took the gold price itself as its main indicator (there was loosening on gold dips and tightening on gold jumps), and certainly by the late 1980s or early 1990s the Fed made a low inflation rate its target. Meanwhile, the very considerable tax cuts of 1981 and 1986 found their match in equally considerable spending cuts in the 1990s, such that by 2000, there was a budget surplus in conjunction with the lowest level of federal spending (as a percentage of GDP) since 1966.

What was demonstrated over the Bretton Woods era once again became manifest and apparent over the Great Moderation: policy that aims to keep the real sector considerable in extent and scope, and based on a medium of exchange that changes little in value per unit, will see a persistent rush toward investment and other real activity, while gold (not to mention oil, commodities, land, durables, art, and any number of other classic hedges) will be quickly abandoned for the long term.

Never let prosperity go to waste

The famous cliché of our Great Recession is the 2009 Rahm Emanuel statement that "you never want a…crisis to go to waste." This gets things exactly wrong. You never want the great runs of prosperity to go to waste. This is the lesson of the huge quarter-century booms that followed World War II and the initiation of the Ronald Reagan economic policy in the 1980s.[12]

During postwar prosperity, the matter of restoring the international gold standard that had gone by the wayside with World War I was never fully attended to. Bretton Woods happened to be a very nice mechanism for taking care of this important business. But it seems that the years of sweet growth during postwar prosperity inured people to the idea that monetary arrangements are not so important, that prosperity is an engine in and of itself, that experts and such can be counted on in any monetary regime to make sure that that end of things can be taken care of sufficiently.

The 1970s proved that all this was complacency. Monetary arrangements are essential. Get them wrong, and things in the real sector will go haywire fast, and for the duration. And the control is gold. If in the process of unfettered decision-making, individuals see little reason to buy, hoard, or speculate in gold, the monetary system will be a good one, and the real economy will be in clover. If, on the other hand, by the same process individuals see substantial reason to buy, hoard, or speculate in gold, the real economy will be in bad straights—and probably in the process of being displaced by government.

As it happened, the Great Moderation saw a reversion to both the real economic and the gold norms of postwar prosperity. And yet the same complacency took hold of policymakers in this latter era. There was assent on the matter of targeting gold for the moment in the operations of monetary policy. But as went formalizing the whole thing and making gold an official basis of the monetary system—this never happened.

In the 1980s and especially the 1990s, the Federal Reserve and its supporters got rather ostentatious about not formally reforming the monetary system. Chair Alan Greenspan was somehow widely regarded as a "genius"; he and Bill Clinton Treasury men were on the cover of *Time* as "The Committee to Save the World"; Bob Woodward's 2000 book about Greenspan was called *Maestro*. The trappings of success in monetary policy (and again this success 1982-2002 was effectively indistinguishable from a simple taking of gold price signals) created momentum in the direction of not formalizing any reform. If geniuses are readily found to run monetary policy, what need is there for reform and strictures?[13]

The latter years of the Great Moderation saw a strange phenomenon. The price of gold marched up steadily from the $300-$350 norm which had been holding for so long, to $800 by 2007, and then to the marks north of $1700 in our own day. Monetary policy was by its own lights unduly loose the whole while. Even by the inflation target, in the early and mid-2000s (which is to say some time before the Great Recession), rates were "too low for too long," a now-common phrase brought into being by the work of Stanford economist John B. Taylor, father of inflation-targeting.[14]

As should be expected, the real sector was feeling pressure from that of the government as the gold-price march proceeded. There were modest tax cuts in the early 2000s, but federal spending was powering forward. The spending level of 2000, of 18.2% of GDP, turned out to be a trough. Spending crossed 20% in 2007 before increasing by fully another *quarter* (as a percentage of GDP) as the Great Recession era of 2007-12 persisted.[15]

It therefore becomes a matter of course to suppose that had the price of gold been stabilized by an official reform of the monetary system in the 1980s and 1990s, it would have been impossible for the slow-growth 2000s to occur, let alone the Great Recession that topped that decade off. Had, for example, the United States guaranteed the dollar to all holders as a convertible currency at $350 an ounce at some point in the heady days of the first two-thirds of the Great Moderation, it is quite impossible to believe that the Fed would have held rates "too low for too long" in the aftermath of the minor 2001-02 recession. Further, had the Fed not held rates too low for too long, the federal government would not have been so confident about the prospect of financing its spending and deficits—that sector would not have been so ambitious in its expansion in these years.

If the complacency during postwar prosperity, which took the form of indifference about the logical culmination of Bretton Woods toward gold, ultimately gave us the stagflation era, it was complacency of a very similar variety during the Great Moderation that yielded the Great Recession. Here is the cycle: postwar prosperity—stagflation—Great Moderation—Great Recession. The only comfort that may perhaps be taken here is that the booms seem to be of longer duration, a quarter century, as opposed to the dozen years (stagflation) or half a decade (the Great Recession so far) of the bust periods.

It is perhaps tempting to see in this pattern the old suspicion about the gold-standard days of the nineteenth century: these were times of "boom and bust." Yet it is striking that the famous "busts" of the nineteenth century seem to correlate to *departures* from the discipline of gold. 1819 came on the heels of the severe overprinting and suspension of convertibility in the war years of 1812-15. Ditto 1873, likewise on the heels of severe overprinting and suspension of convertibility in the war years of 1861-65. And 1893 occurred just as the United States was monetizing in a major way a non-gold medium (silver). Departure, departure, departure from gold fed right into the major busts of the old days. Surely it was not the gold standard that led to the notorious and oft-invoked "cycle" of boom and bust, but tiring of it that did.

And so it is with our contemporary cycle of good times and bad. It was not Bretton Woods and its excellent means for a temporary operation under the auspices of a joint dollar-gold standard that necessitated stagflation. Rather, it was shortsightedness (with a dash of condescension towards gold) about the opportunity at hand to let this temporary mechanism fade away in favor of a classical gold standard that gave us stagflation. Let it be said: lack of seriousness and lack of foresight, plus insouciance and presumptuousness toward the "reactionary" monetary reform possibilities given postwar prosperity and Bretton Woods, brought about the bust of the 1970s.

As the 1970s wore on, the revulsion towards stagflation became so unbearable that by the early 1980s a simulacrum of Bretton Woods had to be engineered by policymakers. Americans whose living standards were taking such unconscionable hits over the long 1970s at last would not have it any other way. And yet while the next boom came with the dollar stable against gold (and the fiscal sector in retreat against the real), the same process of forgetting and indifference toward the final opportunity came to the fore. Once again, now in the Great Moderation, the table was set for a *formal* return to gold, and nothing occurred. As a result, we got the Great Recession in the stead of stagflation. To speak in terms of the old venerable aphorisms, it turns out that in this most important series of episodes, history came first as farce, only to repeat itself as farce; and those who did not learn from the mistakes of the past indeed were condemned to repeat them.

It is interesting that internationally, there has been some action taken to create the conditions of a de facto gold standard. In the realm of fixed exchange rates (one of the great correlates of a gold standard), China has struggled manfully since the 1990s to enforce them with respect to its currency (the RMB) and the dollar. This represents China's effort to get a legitimate price structure, and investment moving in the right direction, in the command economy inherited from Mao. Thus in the 1990s, China identified an effect of the gold standard (fixed exchange rates), resuscitated it, and then watched as the economic results in the formerly near-destitute homeland came in as nothing short of epic.

Likewise the creation of the euro, as long taught by Robert Mundell, represented the best hope for the dollar to maintain itself as a stable currency. If there were another currency with as large and roughly as prosperous a transactions area as the dollar (the thinking at the origins of the euro went), in the form of the euro, the masters of the dollar would not be tempted into devaluation. There would be too great a currency to bail out to if the dollar got unserious.

Thus during the years of the Great Moderation, the RMB instituted *fixed exchange rates* and the euro a form of a dollar *anchor*. These had always been the two major effects of the classical gold standard, and both were made explicit in Bretton Woods. You can nearly touch the yearning for the halcyon days of the international gold standard (as well as for American leadership on the issue) in the main monetary developments that took place during the Great Moderation that were in fact formal. But the all-determining U.S. stuck with fiat principles, and the farce that has been the Great Recession must needs came.

Arguing for gold now

What is to be done—today? The first thing to be accomplished is to absorb the grand economic lesson of post-World War II history. This is that whatever tales have been told about such things as the success of Keynesianism in the 1950s and 1960s, the diminishment of living standards in the Ronald-Reagan-cum George W. Bush economy, and the responsibility of "deregulation" for the Great Recession—all that—must in seriousness be swept aside so that the true overriding message that the economy has continually been delivering be discerned. This is that gold must be attended to; and when it is, sterling results come, while when it is not, one has to deal with the kind of busts that make people reminisce about the Great Depression.

The fact of the matter is that we are in a position to argue for the gold standard on the basis of contemporary history. The most important argument for gold at this juncture in time is that: **Gold delivers**.

The correlation between gold's stability at a low price with great economic booms, and gold's manic (largely upward) swings during extended runs of substandard real performance is too much to be dismissed. The economics of the correlation are in any event not difficult or esoteric. Low gold (in a free market) means that real-sector investment and transaction opportunities are splendid. High gold (gold being an asset class, let it be remembered, which pays no coupon and has considerable carrying costs) means that the real economy and its profit potential must be in the doldrums, probably muscled down to size by government.

This leads to another correlate argument about returning to gold. Above all: **Times of prosperity are the easiest for a return to a gold standard**; which includes this lemma**: Times of prosperity must be taken advantage of as goes a return to gold, or else a grand bust will occur**.

For all the cogitation about transitioning out of Bretton Woods that occurred across the universe of international economics in the 1960s, and for all the cogitation that did not correspondingly occur across that same universe about getting out of the temporarily stable fiat-money system of the Great Moderation (excepting, perhaps, the thinking surrounding the RMB and the euro), the time has come to recognize that the next run of prosperity must not be wasted in indifference toward international monetary reform in the direction of gold.

It would have been easy as pie in the Great Moderation for the U.S. to fix the dollar to gold at $350 an ounce. We may even be permitted to suppose that the small consumer-price inflation scenarios of this era, of some 3% per year, themselves represented little more than a hedge against the fiat nature of the monetary system. 3% inflation per year still results in a doubling of the price level (and a 50% devaluation of nominal assets) every generation, a manifest harm; moreover, since financial products must be developed to hedge this problem, even a small secular inflation of this order is sufficient to diminish the growth in the non-financial markets for goods and services. This is not even to mention the rather extreme exchange-rate volatility of the period—the otherwise stable Great Moderation—that occasioned such problems as the hollowing out of U.S. manufacturing and ultimately the Japanese bust of the 1990s.

That is to say: had the United States gone on gold back in the 1980s or 1990s, it is not merely clear that the Great Recession would have been staved off. It is also prospective that growth would have been even higher than the nice 3-4% yearly rates that were clocked during the Great Moderation proper. The same may reasonably be said of the economy of the Bretton Woods era. The trade-offs for not going fully on gold during prosperous times come in two forms: one is the stalking horse of an extended period of distress á la stagflation and the Great Recession; the other is further heights of wealth forgone in the periods of prosperity to begin with.

If these claims seem to have the ring of the inordinate, it must be kept in mind that the nineteenth century saw immense runs under circumstances where the United States was primed to get on gold and then in fact did so. The yearly growth rate from 1866 to 1893—a 27-year period precisely comparable in length to postwar prosperity and the Great Moderation—was a whopping 4.3%, a full point higher than in the heralded post-World War II runs. At the beginning of the post-Civil War period, the United States was not on gold, though clearly had the opportunity to beat a path to gold. The U.S. seized this opportunity, after a minimum of dithering, and realized a formal commitment to gold in 1879, inaugurating what is statistically easily the greatest dozen years of economic growth ever achieved in this nation's history. (The economy doubled in size over twelve years.) This epic run, all under gold, was sufficient to render this nation the largest economy in the world, a status it has continuously held to this day.[16]

In another 28-year run, 1833-61, similar things happened. This began during a season of prosperity, with the United States considering whether to formalize its gold standard more firmly. The decision was made in the affirmative, and over these 28 years at last broken by the Civil War, real growth was 4.1% per year. Whatever our affection for bygone postwar prosperity and the bygone Great Moderation—and this is not to diminish the very nice records of economic performance achieved therein—they really do not compare, over the sweep of American history, to the most serious eras of economic growth. And each of these was a *locus classicus* of the gold standard.

All of this however must have the aspect of idle chatter, in that one thing that is unduly obvious today is the persistence of, if not the Great Recession itself, then a sluggishness born of Great Recession that if continued shall in due time bring an end to the American dream. Such of course was stagflation, and it was conquered. If somehow the monetary and fiscal sector would diminish themselves over the next few years, we would surely see nice real growth and a fall in gold to a low, stable level (say, $600 per ounce). At last it would be possible once again to make de jure the de facto—a low, stable price of gold—thereby institutionalizing prosperity, as it nearly was in the nineteenth century. America's leaders would do well to recognize that it is their responsibility to execute the imperative of the Stephen Foster song: "Hard times come again no more."

It is so easy to return to gold during the high times that it is tempting to wait until they return to reform the monetary system. The current crisis, especially given its international dimensions and aspects, does not seem to afford us the luxury of waiting. Perhaps the crisis cannot be snuffed out until gold takes its place de jure in monetary affairs.

It is an unfounded argument against the gold standard today that gold has shown itself too volatile, and too reflective of arbitrage and speculation opportunities, for it to be the way forward in our current distemper. Gold has been on the rise and volatile of late precisely because world monetary authorities, above all the Fed, have made it abundantly clear that they will not be taking gold into account in their prosecutions of policy. The price of gold has thus represented a worldwide "vote" (as financial commentator David P. Goldman is wont to say) on the advisability of the fiat blowouts that have attended the failed efforts to slip the Great Recession.

If the Fed and Treasury were to make serious (and non-interventionist) indications that a stable price of gold was desired, it is perfectly conceivable that the world gold markets would respond in kind with a steady drop in the price of gold, to some moderate level below current marks. Moreover, if in tandem the federal government of the United States were to make credible commitments about reducing its footprint on the economy—again, all this is so in the realm of practicality that it was achieved in the 1980s and 1990s—there would be credibility lent to the idea that the real sector stood to run and that the medium of exchange of that real sector would retain soundness.

If, however, one side of this policy mix proved uncooperative—if in the face of fiscal tightness there were monetary looseness, or in the face of monetary stability yet more fiscal expansion—it is unlikely that the real, which is to say the ex-government, sector as an asset class in toto would overwhelmingly attract funds from the great hedge that is gold. Thus gold would not fully get reduced to the low and stable price that would be necessary for a convertibility regime to be successful. If gold is always going up or down, and especially if it seems primed to go up, convertibility regimes stand to get arbitraged to death.

The moral is that forcing an unwilling government on gold will lend ammunition to the opponents of gold. It will create the illusion that gold is unstable as a monetary basis. The redemption price could not be set at or below the current price, in that the government still has its sights set on its own expansion, an effect of which must be further private increases in the gold price and hence those arbitrage opportunities. If, on the other hand, the redemption price were set above the current market price of gold, the government would be given an all clear towards its own expansion, justifying that high price which would be reflective of a sick real sector.

A gold standard is incompatible with a government bent on major displacement of the real economy. Government could perhaps be wooed toward gold, however, if it is made clear that economic growth is so high for so long under gold, that even the most modest taxation will reel in a very great deal of resources for the government. This is not to mention the enormous seignorage wealth that comes to a government that supervises a good gold standard. Under gold, in other words, the economy will boom, the responsibilities of government for the care of the public will decline, and new possibilities of quite lavish government finance will come into season. If government is reluctant to take steps toward gold at the current time, perhaps it is because government is not confident about, or does not know, the considerable advantages under a regime of gold that will accrue to it.

Staying content with the current mediocrity, that of more fiat feats and more taxes, regulation, and spending, all in the context of minimal growth, will eventually cause changes. We should not be so sanguine as to believe that the retrospectively acceptable transition from stagflation to Great Moderation stands to replicate itself after due time with the Great Recession.

American dominance was the predicate of the ease with which the United States could choose, through a simple flick of the policy mix, to put an end to stagflation in favor of the Great Moderation. No doubt such an opportunity still presents itself today, but with every passing year of acute international exasperation at U.S. macroeconomic management and stubbornly declining living standards, it is likely that in the near future there will be a consortium of powers that will force the gold standard on the United States.

This could take any number of forms (alternatives are outlined in Rickards's *Currency Wars*). In all it might turn out to be a salubrious thing for the United States to watch as a group of non-dollar major currencies re-link to gold and thus make the dollar truly undesirable for the first time in centuries. But there is also the possibility that an ex-U.S. alliance of nations that attempts to return to gold would not entirely pull the whole thing off. There could be huge demands for gold, for example, so as to reap big nominal dollar returns, creating a flight of capital from the real sector worldwide and a major depression. Alternatively, the United States could default on its debt on account of a decline in its credit facilities with the rise of an international gold standard, and with these debt instruments in so many important accounts worldwide, the consequences could be severe.

In other words, easy speculation about a gold standard forced upon the United States in the upcoming years yields a few promising and probably a few more disturbing scenarios. This qualifies as another major reason that the United States must return to gold today. It is not merely for the sake of its own prosperity. The U.S. should make the dollar convertible to gold as soon as possible as well for the sake of a harmonious international monetary system and world economy.

On its creation in 1913, the Federal Reserve (with five of its twelve banks down the spine of the prairie) was an iteration of Henry Clay's American System of the century before, itself an attempt to pull the nation inward, away from the coasts and their cosmopolitanism to the comfy bosom of the interior, on whose basis the nation might prosper undisturbed.

In the offing, the twentieth century brought immense new responsibilities of an international nature to the managers of the dollar. The learning and adaptability curves have proven to be of long arcs. For some reason—perhaps it was parochialism and the old pastoral, petty-commerce Jefferson-Clay tradition—the United States proved slow to concede over the course of its epoch of predominance that international monetary leadership is a responsibility that necessarily comes to the U.S. with any "American Century." The lessons were very nearly grasped twice, in postwar prosperity and in the Great Moderation, if fluffed and fumbled at the last moment to quite awful consequences. If we have one more chance in the near future at inaugurating another one of those multi-decade booms, our first obligation as the thing gets going shall be to formalize the dollar as convertible to a fixed weight in gold.

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[1] Benn Steil and Manuel Hinds, *Money, Markets and Sovereignty* (New Haven: Yale University Press, 2010), 9-10.
[2] See the historical prices of gold at www.kitco.com.
[3] For foreign GDP levels, an implied growth rates, see stas.oecd.org.
[4] "Central bank/treasury stocks (in metric tonnes fine gold)," World Gold Council, www.gold.org.
[5] This episode is discussed in Chapter 3 of my own book, Brian Domitrovic, *Econoclasts: The Rebels Who Sparked the Supply-Side Revolution and Restored American Prosperity* (Wilmington, Del.: ISI Books, 2009).
[6] In the thick of the 1960s boom, France famously asked to redeem extraordinary dollar-gold claims, a problem which could have been smoothed out had the United States talked and acted like it was serious about returning to a classical international gold standard in the near future. For U.S. GDP levels, see www.bea.gov.
[7] CPI data from www.bls.gov.
[8] Unemployment data from www.bls.gov.
[9] Stock and oil price data from the "Fred" series at research.stlouisfed.org.
[10] James Rickards, *Currency Wars: The Making of the Next Global Crisis* (New York: Portfolio, 2011), 94.
[11] Robert L. Bartley, *The Seven Fat Years: And How to Do It Again* (New York: The Free Press, 1995), 211.
[12] "Rahm Emanuel: You never want a serious crisis to go to waste," http://www.youtube.com/watch?v=1yeA_kHHLow.
[13] Domitrovic, *Econoclasts*, 251.
[14] See "More on 'Too Low for Too Long,'" Economics One: A Blog by John B. Taylor, Jan. 12, 2010, http://johnbtaylorsblog.blogspot.com/2010/01/more-on-too-low-for-too-long.html.
[15] For federal budget information, see the Historical Tables at the Office of Management and Budget, http://www.whitehouse.gov/omb/budget/Historicals.
[16] For pre-1929 U.S. GDP, see http://www.measuringworth.com/usgdp/.