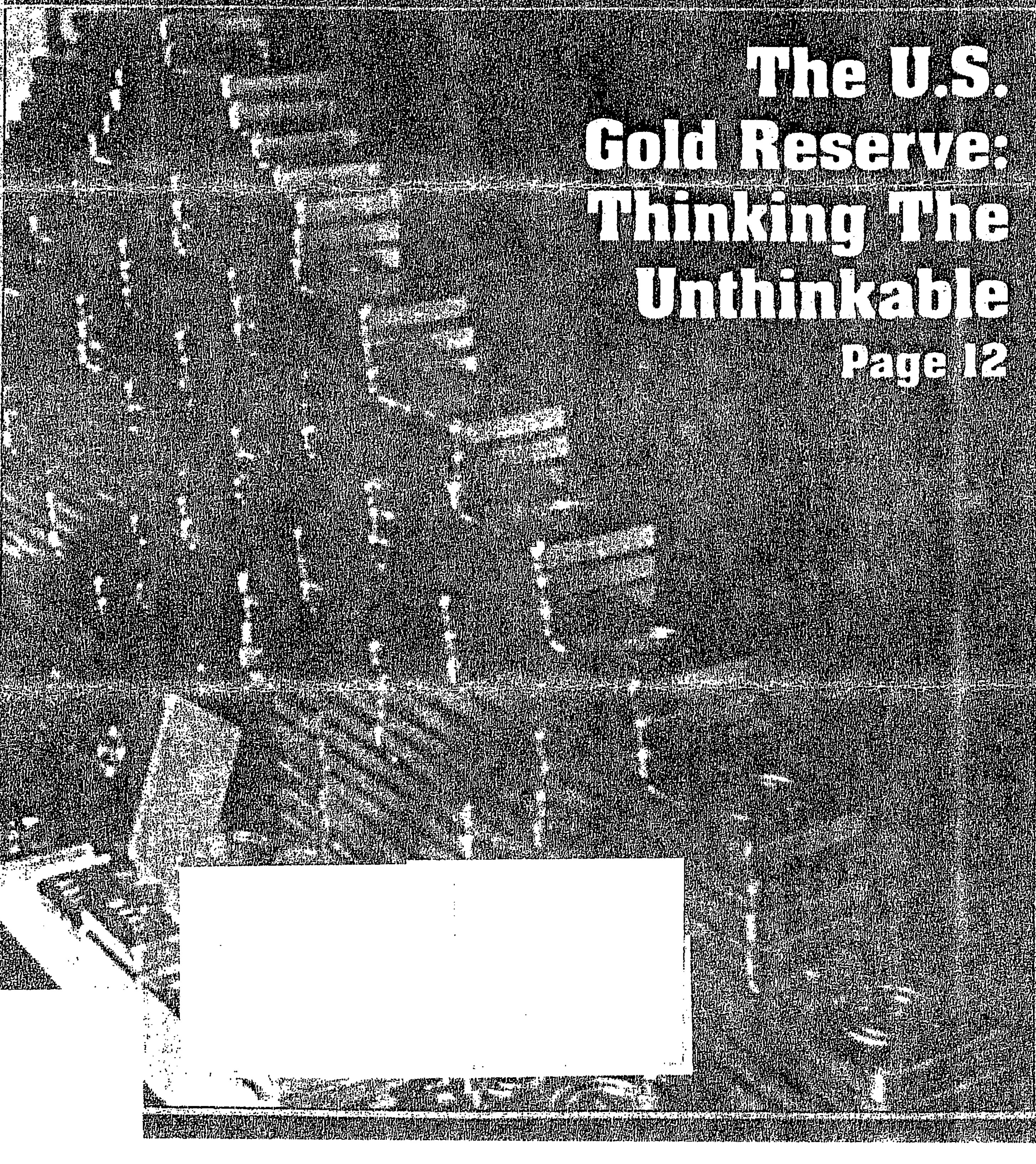
INTERNATIONAL
July/August 1994

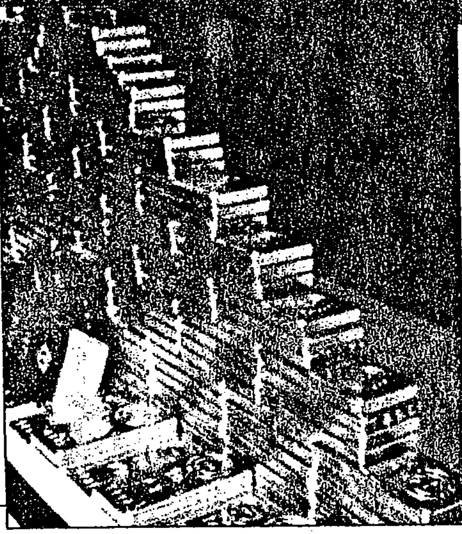
MONEY & POLITICS

DEDICATED TO FREE MARKETS, FREE NATIONS AND FREE MEN



The U.S. Gold Reserve: Thinking The Unthinkable

Page 12



THE U.S. GOLD RESERVE: THINKING THE UNTHINKABLE

By James J. Turk

Over the past few years, I have become acquainted with a wealthy, retired American industrialist who has an interesting story to tell. To preserve his privacy, I will call him Andre, which is not his real name.

Andre was born in New York before the First World War to wealthy Jewish parents who had only recently emigrated to the United States. He was educated in both the United States and Europe, speaks several languages fluently, and is as comfortable in any European capital as he is in any American city. He has three homes in the United States, and two or three more in Europe.

Andre is a "man of the world" in the positive sense in which that phrase can be used. That is, this phrase reflects his vast knowledge and keen perception of world affairs, and over the years, I have come to deeply respect his wisdom.

Andre is also well connected. His library is full of photographs taken of him meeting world leaders. Seeing this gallery is like viewing a who's who in government and business. One immediately understands from these photos that here is a man who was close to world events for decades.

Interestingly, the photos stop in the mid-1960s, but it is here that his story begins. Andre sold all of his business interests and retired around age 55.

> *The U.S. government had not undertaken a proper audit of the gold since President Eisenhower was in the White House in the 1950s. Ed Durrell's argument was simple. If the gold was truly there, then commission an external firm to properly audit the gold to prove that it exists.*

As he explains it, he felt that he could no longer devote sufficient time to manage his diverse businesses. The changes being inflicted on the United States by President Lyndon Johnson meant that Andre would now need to spend all of his time managing the wealth he had been able to accumulate. In his view, the economic and monetary order by 1965 was changing, and he would have to change as well.

The transition was made within a few years. He sold his business interests and most of his stock portfolio. By the late 1960s, real estate in Europe and the United States and investments in gold mining companies became the two pillars of his investment portfolio. In the mid-1970s, he also started buying gold bullion. It was during this period that Andre had the occasion to meet Edward Durrell, one of those legendary figures in the sound money movement protesting, even rebelling, against American government policies that were destroying the purchasing power of the dollar.

Ed Durrell believed that the Federal government was not being honest with the American people. He believed that substantially all of the gold held by the U.S. Treasury had been dishoarded and he began to make his views widely known in the 1970s. He contended that the U.S. gold reserve (which is presently reported to be 262 million ounces) was vastly overstated, and that this deception was being perpetrated on the American people by successive U.S. administrations either ignorant of the truth or afraid to tell the truth.

Ed Durrell's evidence was largely circumstantial, but nevertheless part of it was also somewhat compelling. For example, he noted that the gold disposed by the U.S. government by auction in the late 1970s was coin melt quality, i.e., the gold that had been confiscated in the 1933 seizure by FDR and melted into bars less than 99.9 percent pure. Ed Durrell believed this lower grade gold was sold because the pure bars were missing.

There were other examples. Ed Durrell noted how the *Financial Times of London* had unceremoniously and inexplicably fired its long-standing business and economics reporter, W. Gordon Tether, once he reported in that paper the allegations that the U.S. gold reserve had been surreptitiously dishoarded. Ed Durrell's point was that a cabal in the U.S. government did not want the truth to emerge about the missing gold, for obvious reasons. Most persuasive, however, was his argument about auditing.

The U.S. government had not undertaken a proper audit of the gold since President Eisenhower was in the White House in the 1950s. Ed Durrell's argument was simple. If the gold was truly there, then commission an external firm to properly audit the gold to prove that it exists. His argument sounds logical and simple enough, but curiously, the U.S. government always refused. Moreover, the excuses given were not credible.

The excuse most often used by the U.S. government was that an audit was too expensive, which is really no excuse at all. First of all, even if the audit had cost several million dollars, this amount is insignificant compared to all the money spent each day by the government (much of which we all know from reports of the Grace Commission is routinely wasted).

Further, isn't a few million dollars a reasonable amount of money to spend to ensure that the U.S. government's most important monetary asset is secure and intact? Besides, wasn't it worth spending a few million dollars to complete the audit just to rebuke Ed Durrell and to prove him wrong so that he would no longer be a thorn in their side?

When viewed in this way, the candor of the U.S. government makes one wonder. Was the U.S. government being obstinate, or did it really have something to hide?

Andre thinks the U.S. government did, and still has, plenty to hide. He thinks that Ed Durrell was right and that most of the gold is missing. Here is how Andre tells it.

In his view, Lyndon Johnson was absolutely the worst President that this country ever had the misfortune to elect. Andre believes that Johnson was a man with no scruples or conscience, and little sense of right or wrong. This disparaging view is similar to that portrayed in some of Johnson's less known biographies. To Johnson, power was the only truth. But as Andre explains, not only was Johnson despotic, he was stupid.

Although he can't prove it (and nobody can until a proper audit of the U.S. gold reserve is once again completed), Andre believes that Johnson was the victim of his own megalomania and the dupe of some conniving people who were advising him at the time. To understand his argument, you have to appreciate and understand the circumstances prevailing in late 1967 and early 1968.

The Vietnam War had rapidly escalated, and the protests had already begun. Johnson's credibility was being questioned not only on foreign policy, but domestically as well. The U.S. government's commitment to maintain the gold standard then in effect was suspect, and the gold reserve had declined from 442 million ounces in December 1964 to 370 million ounces by November 1967 in response to the growing demand for redemptions at the $35 rate of exchange then in place. In short, the environment by the end of 1967 was fractious, and Johnson's grip on power was dwindling. Because power was his life, Johnson was forced to act.

Understanding these circumstances as well as Johnson's weaknesses, one or more people with access to Johnson's ear (if Andre knows who they are, he hasn't told me) presented Johnson with a scheme. They told him how he could defend the dollar as the grand deed to bolster his flagging popularity and win back the support of the American people.

All he needed to do was flood the London market with gold, thereby more than satisfying the growing demand for redemptions of the dollar. They led Johnson to believe that once everyone realized how much gold was available, the demand for dollar redemptions would decline, and everyone would be satisfied holding dollars again instead of gold.

According to Andre, Johnson then concocted a secret plot. The entire U.S. gold reserve, then over 400 million ounces (excluding the 15-20 million ounces of coin melt gold which could be determined to be gold from U.S. reserves), would be shipped to the Federal Reserve in New York and the Bank of England in London to be dumped on the market to teach a lesson to the speculators. Not only would there be more than enough gold to meet the growing demand for dollar redemptions, the gold price would drop. The Federal Reserve and the Bank of England would not immediately sell dollars and buy gold, thereby allowing the gold price to fall momentarily below $35. Once the speculators were crushed in this way, the Federal Reserve and the Bank of England would step back in to buy the gold under $35 per ounce and then surreptitiously return it to the U.S. Treasury with no one being any the wiser. Only it didn't work out that way.

Over a period of several weeks in early 1968, the gold was secretly transferred and dumped on the market, but to President Johnson's shock and horror, the market absorbed it all. He had been duped. The people who concocted this plan knew that their group had more than $14 billion of resources (400 million ounces times $35 per ounce). They therefore willingly exchanged their dollars for the gold dumped on the market. The rest of the story is already well known.

In March 1968, the international monetary system, in effect since the 1944 Bretton Woods Agreement, was abruptly ended and replaced by the two-tiered gold system. There would now be a free-market gold price, higher than the $35 official rate. Further, the U.S. government would no longer

– Continued on page 17

The Misperception Of Risk

Continued from page 4

best opportunity for capital gains?

The obvious answers underscore the fact that contrarians are not only generating better returns – they're generating them with less risk! There are many ways to prosper in the financial markets, but following the crowd is not one of them.

Contrarian thinking means investing contrary to the crowd psychology. That means one of the easiest ways to determine whether an investment is becoming timely or not is to ask "the Joneses" how they feel about it. (In technical jargon, this is known as the "next-door neighbor indicator.") If the Joneses feel the investment in question is a good buy at the moment, chances are that it's too late to buy and maybe even time to consider selling. If, however, the Joneses feel you've taken complete leave of your senses to even ask such a question, you are probably looking at a decent opportunity.

When the Joneses panicked after Black Monday, the contrarian jumped into the stock market with both feet. Today, of course, the Dow has more than doubled since then, even after this year's mild correction. And when the Hong Kong market collapsed a couple of years later following the crackdown in Communist China, *60 Minutes* proclaimed that not just the investment capital but even the investors themselves were leaving Hong Kong. At that point, as a contrarian, you could have bought the biggest bank in Southeast Asia, the Hong Kong Shanghai Bank, at 50 cents a share. It has since risen more than tenfold.

Yes, it's certainly a pleasure to see your investments rise – especially when you do it with less risk. It takes intelligence and no small amount of courage to buy something that nobody else will touch with a ten-foot pole, or to sell something that everyone else is buying.

And there's one other thing about being a wise contrarian investor – it's based on logic, not emotion. Too many of us make decisions based on emotion. When it comes to our investments, too often we jump on the bandwagon, chasing what was the best investment last year or last month. And too often this emotion-based decision process leads to disaster. To be a contrarian investor is not to be an old curmudgeon – it's a strategy based on logic, reason, and discipline.

> *It takes intelligence and no small amount of courage to buy something that nobody else will touch with a ten-foot pole, or to sell something that everyone else is buying.*

Sometimes, of course, there is no clear consensus about the direction of the financial markets. During such times it is unlikely that prices will move dramatically in either direction. At the moment, for example, stock market sentiment is roughly 50 percent bullish and 50 percent bearish. The contrarian can therefore conclude that stocks in general will neither advance nor decline by a substantial percentage in the weeks ahead.

Once a consensus does develop, we contrarians will begin to position ourselves to counter the prevailing sentiment. Because if you hear too many people saying the same thing and touting the same investment, whether they're your friends and neighbors or even the so-called "experts," you might want to think about doing the opposite.

And you would be wise to heed the words of J. Paul Getty, a contrarian if there ever was one: "Buy when everyone else is selling, and hold until everyone else is buying. It is more than just a catchy slogan. It is the very essence of successful investment." ▲

The U.S. Gold Reserve: Thinking The Unthinkable

Continued from page 13

redeem dollars for gold because as Andre explains, the U.S. gold reserve had been depleted by Johnson's insane folly. There no longer was enough gold to make redemptions.

The so-called speculators, and their friends who advised the President, had made a fool of Johnson. The $14 billion they invested in gold immediately rose in value as its price climbed above $35 per ounce.

It is also known that shortly after the March 1968 meeting establishing the two-tiered gold price, President Johnson surprised the world by announcing that he would not run for a second term. Andre believes this humiliation over the gold to be the real reason President Johnson decided to step down from the pinnacle of power. Subsequent administrations unwilling or afraid to deal with the truth, have continued the cover-up.

It's a great story, but is it true? Before dismissing it out-of-hand, consider this. We all know now that President Johnson lied about the Gulf of Tonkin incident. It has been proven to be a phony event, staged by the U.S. government to justify greater involvement in Vietnam. If Johnson lied about that, who's to say he didn't lie about the U.S. gold reserve?

I suppose the only answer lies with an audit. The U.S. government says that the GAO has inspected the gold in the U.S. gold reserve, but an inspection is not the same as a full audit. Until a full and independent audit is completed, we will never know whether the gold is there or not. The few million dollars that it would cost for the audit seems a small price to pay for the peace of mind knowing that the gold is there. And if this essential monetary resource isn't there, I would rather not think the unthinkable. ▲

James J. Turk, a noted authority on precious metals and monetary matters, is editor and publisher of The Freemarket Gold & Money Report, *P.O. Box 4634, Greenwich, CT 06830.*