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# GOLD MANIA–
# Capitalism's Fever Chart

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The orgy of gold buying that pushed the price of gold up to well above $400 an ounce last autumn, and the subsequent hectic speculation that has kept the price fluctuating around that level, resembles the kind of mania that in the history of capitalism has often been the prelude to a major financial crisis. It would be a foolhardy and idle exercise to try to forecast the future course of the current speculative madness. What is important, rather, is to recognize that this drastic increase in the price of gold—now at a level more than ten times that of 1971—is a symptom, one might say a fever indicator, of the deep-seated troubles facing the capitalist world. At a minimum, the recent behavior of the price of gold clearly demonstrates how quickly panic can overtake and shake up financial markets as the more sensitive sectors of the bourgeoisie become increasingly aware of the shoals lying ahead for the leading capitalist nations and for the international monetary system.

The linchpin of the international monetary system during most of the years since the Second World War was the maintenance of a fixed *dollar* price for gold. At the Bretton Woods Conference in 1944 it was agreed that gold would be valued at $35 per ounce in all official transactions. This was intended to provide a firm basis for foreign-exchange stability, which in turn would facilitate the flourishing of international trade. And despite many tensions and growing problems, the system worked

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fairly well until the early 1970s. True, the ability to maintain such a fixed price was at times threatened by speculation in the private gold markets, but in the main the leading capitalist nations were able to intervene sufficiently in those markets to prevent the price from reaching a level much above the magic $35. As for official transactions between central banks, the system functioned as planned so long as the United States was able and willing to live up to its commitment to convert, upon the request of foreign central banks, dollars into gold at the fixed price.

The postwar international monetary system got off to a good start because during most of the first two decades after the war the United States was in a clearly dominant position. At the end of the war the country was by far the leading manufacturer, foreign trader, international banker, and, last but certainly not least, global military power. At the same time most of the government-held gold of the capitalist world was in the vaults of the U.S. Treasury Department. The other capitalist nations, notably the countries devastated by war, had relatively little gold and were desperate for dollars to buy food, coal, and manufactured goods from the United States. Under such conditions, the enshrinement of the dollar as *the* international medium of exchange appeared to be a reasonable and logical substitute for the more traditional medium, gold.

In the corridors of power one could hear repeated with increasing frequency Keynes's put-down of gold as no more than a "barbarous relic." Who other than jewelers and dentists needed gold when the dollar was just as good, if not better, as an international means of payment? What was conveniently overlooked, especially by U.S. "experts," was that the power of the dollar was rooted in the hegemonic position of U.S. capitalism. The fact is that the dollar started to lose its luster just as soon as rival imperialist powers began to get back their strength and their giant corporations and banks once again became serious competitors in the international arena.

By that time, however, the contending imperialist powers were caught in a trap. At $35 per ounce there just wasn't enough gold in governmental (or central bank) coffers to finance the rapid expansion of international trade with its accompanying inflation of world prices. For this, alternative means of payment were urgently required. And, as it happened, the United States was happy to meet this need through flooding world markets with dollars to finance its military bases and imperialist wars; to buy control or influence over weaker nations with military and economic aid; and to facilitate the global expansion of its multinational corporations. When the United States needed more money to pay for these far-flung imperialist activities, it just created more dollars in the form of bank credits. But the more this swelling tide of dollars inundated the foreign banks, the less did these dollars glitter like gold. Gold, after all, is the undisputed repository of value in all markets. Dollars, on the other hand, are merely IOUs that are ultimately valuable only for the purchase of U.S. goods and services. Hence the dilemma for other countries and particularly for rival capitalist centers: in the short run the inflowing dollars were good for business; but, since they were only IOUs the value of this vast and seemingly endless accumulation could at some time in the future collapse.

Foreign financiers had no easy way out of this bind. If they refused to accept dollars as the equivalent of gold, the entire international structure could come tumbling down. So they played by the established rules of the game, made as much profit as they could, and at the same time sought ways to evade them. As a hedge against a possible day of judgment, they kept on converting some of their dollar hoards into gold. The upshot was that the commitment made by the United States under the Bretton Woods Agreement to convert, upon request, foreign dollar assets into gold became an increasingly empty one. This can be seen in the following simple summary:

| *End of* | *U.S. Gold Reserves* | *U.S. Dollars Held Abroad* |
|---|---|---|
| | *— Billions of Dollars —* | |
| 1955 | 21.8 | 11.7 |
| 1971 | 10.1 | 65.6 |

Source: *Federal Reserve Bulletin*, various issues.

Clearly, the U.S. pledge to exchange gold for dollars was plausible back in the 1950s when there was almost twice as much gold on hand as there were dollars abroad. But the continuous and ever larger U.S. balance-of-payments deficits that generated the pile-up of dollars abroad, together with the drying up of U.S. gold reserves, changed all that. The contradiction between the U.S. gold-conversion commitment and the possibility of living up to it kept on growing—until it reached a point of crisis in 1971. By that time, as can be seen from the above figures, the amount of foreign-held dollars was more than six times the U.S. gold reserves. And, facing up to that reality, the United States was forced to default: in August 1971 gold and dollars were declared no longer interchangeable, and the dollar was devalued. (For a fuller discussion of the 1971 crisis see the Review of the Month on "The End of U.S. Hegemony" in the October 1971 issue of MR.)

This unilateral action, soon followed by changes in the regulations of the International Monetary Fund (IMF), effectively removed the $35 lid on the price of gold. The "free" private market took over, and the price leaped upward, reflecting the impact of both the extensive postwar inflation and the devaluation of the U.S. dollar. Once let loose, the price of gold fluctuated widely, moving up toward the $200-per-ounce level by the end of 1974.

The sharp increase and wide fluctuations, however, posed new obstacles to the IMF's aim to maintain some reasonable order in the international monetary system. On the one hand, it had proved impossible to maintain a fixed price for gold as the anchor of the system. On the other hand, gold was still counted as a monetary reserve by the IMF and its members. Given this continued reserve role for gold and the evident desire of many countries to peg the international value of their currencies to gold, it was inevitable that wide fluctuations in the price of gold would be a constant source of disorder in foreign-exchange markets.

The decision was therefore reached by the IMF at the beginning of 1976 to demonetize gold: that is, to reduce and eventually eliminate the role of gold as a medium of international payments and as a currency peg. This step was fully consistent with the desires of the United States. For, despite the actual and potentially even greater weakness of the dollar, it still remained by a wide margin the major reserve currency in the capitalist world. The further gold could be removed from the center of the stage, the more dependent would the rest of the world remain on the use of the dollar.

Once the speculators learned of the plan to demonetize gold, and especially when the IMF started to carry out its program by a measured reduction of its gold stock, the price of gold took a nose-dive. In 1976 the gold price sank by almost half from its previous high—to a price of approximately $108 per ounce. In view of what has been happening more recently in the gold market, it is important to understand that this kind of a decline is consistent with the ordinary rationality of the capitalist market place. The supply of gold offered for sale increased, speculative demand weakened in view of the official program to keep on selling the IMF's gold and to demonetize gold—and the price of gold consequently fell. Nevertheless, the drop of the *U.S. dollar price* of gold did not last long, giving way to sizable increases during 1977 and 1978. This again was "logical" in view of the rapid depreciation of the international value of the dollar in those years. (For this, see the Review of the Month on "Emerging Currency and Trade Wars" in the February 1978 issue of MR.) At the same time, the price of gold in Swiss francs kept on declining throughout 1977 and until late 1978.

In contrast, the behavior of the gold market in 1979 displayed entirely new features. First, the price skyrocketed in spurts which the *Wall Street Journal* termed "near-hysterical." From September 1978 to August 1979 the price advanced by a little over 40 percent, from $210 to $300 per ounce. Then, in a little more than a month, from the end of August to October 2nd, it leaped upward by about 50 percent, from $300 to $447 per ounce.

Second, the rise in the price of gold in 1979 was no longer a simple response to a depreciating U.S. dollar. The gold price increased relative to *all* currencies. No more could the price gyrations be understood as a flight from the dollar. They were now the result of a flight from all the leading currencies: from the French, German, Swiss, and Japanese.

Finally, the upward price spiral was apparently in flagrant contradiction to the law of supply and demand. Throughout this period the IMF continued to sell gold. Then, in addition, the U.S. Treasury began in May 1978 to sell even larger quantities of gold in monthly auctions. Meanwhile, no significant changes took place in the customary gold requirements by industry and commerce. Accordingly, the normal expectation would be that the dumping of gold on the market would push the price down. Yet what happened was just the opposite. *The larger the quantity of gold offered for sale, the stronger demand grew, and the higher the price soared.*

A common explanation for this strange phenomenon is that speculators became wildly irrational. The new price level, however, would not have lasted as long as it has if it were merely the product of manipulation by market operators. Behind it had to be some solid basis of demand: individuals, businesses, and governments that were desperately anxious to build up their hoards of gold, and at unprecedentedly high prices. Behind this, no doubt, lies the conviction of central bankers and other financiers that despite, or perhaps because of, the mystical feature of gold, possession of this precious metal is the ultimate trustworthy medium of exchange in a world beset by seemingly endless inflation and instability of the international monetary system.

Here we need to keep in mind that as a result of the flood of U.S. dollars abroad and the maintenance for years of a lid on gold prices, the gold proportion of the reserves of central banks outside the United States had declined sharply while dollars had become the dominant form of reserves. With the new price level of gold, the situation is reversed: less than 24 percent of the reserves of the leading capitalist nations had formerly been in the form of gold at the old "official" price,* the rest of the reserves being in the form of foreign exchange, predominantly dollars; now, with the removal of an "official" price and the skyrocketing of the gold price, the proportion of the reserves held in gold, if measured in current prices, amounts to almost 60

* After the U.S. devaluation of the dollar in 1971, the IMF raised the price at which central bank gold stock was to be valued to $42.22 per ounce. Then, in 1976, as part of the plan to demonetize gold, the IMF lifted its restrictions on how central banks should value their gold in settling accounts with each other.

percent (according to a tabulation by *The Economist,* October 27, 1979).

Given this situation, the aim of U.S. monetary authorities to eliminate the monetary role of gold (and thereby strengthen the international role of the dollar) is and will remain mere wishful dreaming. *Business Week* (October 1, 1979) quoted a Paris banker who put the point in a nutshell:

> The United States has failed in its efforts to demonetize gold, and what is important is that previously the United States had always succeeded in imposing its views on this sort of monetary question. Now it can no longer do so.

It would clearly be in the interest of U.S. imperialism if gold would indeed be treated by the rest of the capitalist world as a "barbarous relic." But that would be possible only if we had passed the age of economic barbarism. No matter how much economists may rail against reliance on gold as an atavistic throwback, the fact remains that the only viable alternative to an "objective" regulator of the international monetary mechanism would be effective planning and genuine cooperation among the leading nations in the service of a theoretical common good. But this would entail a willingness on the part of all of them to make compromises involving sacrifice of their perceived self-interest, and if four centuries of capitalist history have demonstrated anything it surely is that no such behavior can be expected from societies organized as sovereign nation states. Indeed, experience suggests that the greater the degree of interdependence among capitalist nations, the greater is the need for each to protect its own interests at the expense of the others. And this of course generates not cooperation but competition and conflict which tend to disrupt the harmony of the international system and lead to recurrent periods of disorder.

To be sure, there have been interludes in the history of capitalism when there was more or less order in the economic relations among the advanced capitalist nations. But these have been periods when there was a clear-cut hegemony by one of the powers that could pretty much lay down the law, such as England during a large part of the nineteenth century and the United States in the first two decades after the Second World

War. Now, since the decline of U.S. hegemony, a new era of international economic disorder has emerged, with the gyrations in the price of gold being one of its characteristic symptoms.

The troubles of capitalist societies, however, are internal as well as external. Although the extent of inflation varies from country to country, no country has escaped being infected with the disease. That, combined with a general state of lagging growth and a present or impending cyclical downswing, raises the specter of a world-wide major depression. In these circumstances, it is no wonder that the more nervous capitalist interests have been shifting part of their wealth into nonproductive gold. Seen in this light, the flight from paper currencies is both a product and symptom of the current deep-seated capitalist illness. As we go to press, panic once again seems to be seizing the gold market. This may of course subside, but the forces underlying it are still very much with us and, unless something entirely unexpected intervenes, seem certain to produce more and bigger panics of one sort or another in the period ahead.

(December 12, 1979)

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**Gold, yellow, glittering, precious gold!**
**Thus much of this, will make black white; foul, fair;**
**Wrong, right; base, noble; old, young; coward, valiant.**
**... What this, you gods? Why, this**
**Will lug your priests and servants from your sides;**
**Pluck stout men's pillows from below their heads;**
**This yellow slave**
**Will knit and break religions; bless the accurs'd;**
**Make the hoar leprosy ador'd; place thieves,**
**And give them title, knee and approbation,**
**With senators on the bench; this is it,**
**That makes the wappen'd widow wed again:**
**... Come damned earth,**
**Though common whore of mankind.**

**Shakespeare, *Timon of Athens***

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