Standards Today

A Journal of News, Ideas and Analysis

A publication of CONSORTIUMINFO.ORG GesmerUpdegrove LLP

March-April 2010 Vol. IX, No. 2

CONSIDER THIS:

#63 How Now, Gold Bug?

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Sometimes, its just turtles, all the way down

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Standards cover an awful lot of ground – how big things are; how much they weigh; how fast they go; how much power they consume; how pure they are; how they must be shaped so that they fit together – the list goes on and on. But despite the enormous range of characteristics that standards define, you notice that they all have one thing in common: you can describe them by using the word "how."

In short, standards relate to measurable things. Indeed, the earliest formal standards created in societies everywhere were usually those related to weights and measures. Invariably these were established when trade became more sophisticated than tribal bartering. Ever since, the history of standards has largely been one of establishing ways to define more and more measurable characteristics as they became important and as the scientific ability to test them came along.

There is, however, one exception to this rule. Curiously enough, it involves a standard that is as old as weights and measures themselves. And despite its ancient lineage, nations still can't agree for very long on what measuring stick should be used, or how it should work. This is rather remarkable, given that the standard in question is perhaps the only one that nearly everyone makes use of almost very day of their lives.

That standard, of course, is money – dollars, Euros, renminbi – each one a measure of value.

The problem starts with the fact that while any two people may agree on what it means to say that a given object weighs a pound, the value of the object in Pounds is necessarily in the eye of the beholder. There are temporal issues to address as well. While the weight of the object in question will still be one pound tomorrow if left undisturbed, its value in the marketplace will likely have changed, even if only slightly.

All well and good, you may say, but a standard is the way we measure value, not the value of the object itself. So if it's worth ₤3.01 tomorrow instead of ₤3.00, what's your point? We can still measure the difference (domestically, at least) in new pennies. Fair enough. But consider this: if something's value changes, it must be changing relative to something.

Now what exactly might that be? When we say that the object in question is one meter long, we are more efficiently saying (thank heavens) that its length is the same as the distance that light would travel, in a vacuum, in 1/299,792,458 of a second. With the kilogram, the earth's gravitational force at a certain place and altitude provides our yardstick. But where is that certain something we use as the reference point for that Pound of which you speak?

Tricky, that. Trying to find the reference point for that dollar is rather like finding out what the true foundation of the world might be from the perhaps apocryphal person who famously believed that the earth is a giant bowl residing on the top of an enormous turtle. When asked what the turtle was standing on, she scornfully replied, "Don't talk such nonsense! It's turtles all the way down!"

Determining what the dollar is "standing on" matters, because even if we are dealing with perceptions rather than empiricism, the rise and fall of markets, interest rates, and even nations rests on the perception of the relative wealth and creditworthiness of those involved.

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So it is that people have struggled from the dawn of time with how to measure what is, in fact, an abstraction.

That effort has too often involved forcing the round peg of traditional standards rules into the square hole of monetary policy. When that happens, people time and again have turned to a single gleaming, elemental reference point to give some sort of reality to the value of their dollars and pounds, rubles and francs.

I refer, of course, to gold – the "Mama Bear" of monetary reference points. There's neither too much of it available to be unwieldy to store securely nor too little to go around for everyone to rely on; it doesn't oxidize, so it doesn't require special care to avoid deterioration; its supply doesn't grow faster than the global economy (the opposite is true); and perhaps best of all, it has intrinsic visual credibility – it looks valuable, and desirable, too.

As a result, gold has always provided an appealing option as a reference point for establishing value. Even from ancient times, it has been used far less often as coinage than to back up the credibility of coinage made of lesser metals. Because the amount of gold in the treasury of the sovereign whose mint struck a given type of coin supposedly equaled the amount of coinage placed in circulation, the coins had credibility. Indeed, in some countries in some eras coinage could actually be presented at a mint in exchange for gold.

In the modern era, bank notes have largely replaced coins, but in many cases (as in the United States) those bank notes could be exchanged for actual gold coins, and later for silver. Only in the mid twentieth century were "silver certificates" removed from circulation in the U.S. After World War II, the gold standard was internationally formalized with the dollar as the first link in the valuation chain: under the Bretton Woods treaty, the value of the dollar was fixed at $1/35^{th}$ of a Troy ounce of pure gold, and other nations indirectly established the value of their currency relative to gold via conversion rates into dollars.

Nor was this completely an abstraction. By the same agreement, treaty parties had the right to redeem dollars for actual gold. All this ended in 1971 when an economically beleaguered U.S. President (Richard Nixon) unilaterally dropped out of the treaty. Today, modern nations issue only "fiat currency," backed by nothing tangible at all.

Meanwhile, domestically as well as internationally we increasingly employ less and less to represent more and more - pieces of plastic, or indeed nothing tangible at all - simply digital numbers displaying above ATM keypads, electronic signals exchanged between banks, and debits applied to accounts as we drive at speed through toll booths.

In such a world, one might reasonably ask whether there is any empirical measurement of "value" at all? The answer, I would submit, is "no."

As evidence, witness the enormous increase in the money supply issued by central banks in countries such as the United States during the recent recession. Despite the fact that the value (however measured) of gross national production declined in the U.S. relative to the years preceding the economic crisis, the amount of exchangeable currency (both printed and virtual) was made to increase dramatically. In other words, there was no measurable relationship between the supply of money and any underlying value at all. Instead, the Federal Reserve relied on the marketplace to believe that somehow everything would all work out, with neither the type of catastrophic inflation or deflation to follow that would lead a holder of government debt to suffer.

The result has been a call from a surprising number of quarters to roll the clock back a hundred years and revert to a gold standard, ideally on a global basis. One express goal of such a move would be to prevent a government from issuing more currency and loans than it could pay back if the holders of currency sought to redeem their holdings in gold (necessarily valued now at something like $6,000 an ounce, given the size of the global economy relative to the available supply of bullion).

Superficially, such a suggestion sounds rational. This being economics, of course, there are as many who hold the opposite view, pointing out that in the Great Depression, the speed with which a nation's economy revived after the Crash correlated closely with the rapidity with which it abandoned the gold standard in favor of easing credit. Sometimes, it seems, delinking the currency supply from the value behind it may be a good idea.

Perhaps it would help gold bugs abandon the dream of resurrecting the past to find the future by pointing out one simple fact: if we're going to peg everything to gold, what is it that we're going to peg gold to? Yes, such a system might to some degree rationalize economic relations between countries, but the world as a whole would remain unsupported. Sadly, there simply aren't any more turtles underneath to support whatever value it is we agree to give to gold.

All of which leads me to conclude that arguments over a return to the gold standard only distract us from developing the kinds of standards we really need to ensure the credibility and stability of the financial system. Those standards go by a different names, though. We call them laws and regulations.

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