

MONEY



How the Destruction
of the Dollar Threatens
the Global Economy—and
What We Can Do About It

Steve Forbes

Elizabeth Ames



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MONEY is one of the most misunderstood—and crucial—topics today. Since the United States abandoned a gold-linked dollar more than four decades ago, the world’s governments have become dangerously ignorant of the fundamental monetary principles that guided the most successful economies for centuries.

This extraordinary book shows how today’s wrong-headed monetary policies are setting the stage for a new global economic and social catastrophe that could rival the recent financial crisis and even the horrors of the 1930s. Coauthored by Steve Forbes, one of the world’s leading experts on finance, *Money* shows you why that doesn’t need to happen—and how it can be prevented.

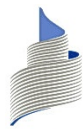
Money explains why a return to sound money is essential for the United States and other nations to overcome today’s problems. Stable money, Forbes and Ames argue, is the only way to a true recovery and a stable and prosperous economy. In *Money*, the authors answer these vitally important questions:

- What is the difference between money and value?
- How does sound money contribute to a well-functioning society?
- How have our money policy errors led to the current problems in global financial markets?
- What can we do now to reestablish the strength of the dollar and other currencies?

Fluctuating “fiat” money, in which governments manipulate the value of the dollar and other currencies, has been responsible for the biggest economic failures of recent decades, including the 2008 financial crisis, from whose effects we continue to suffer. In *Money*, the authors show

(continued on back flap)





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Advance Praise for *Money*

“In this fascinating book, Steve Forbes makes the case for sound money and shows why a money system based on free trade—a system that allows the entrepreneurial dream to flourish—is not just good business; it also makes for a good society. *Money* is a rock-solid argument for the virtues of capitalism.”

—JOHN MACKAY, Co-Founder and Co-CEO,
Whole Foods Market; coauthor of the
New York Times bestseller *Conscious Capitalism*

“*Money* clearly illustrates that sound money is an essential foundation for a free and prosperous society and that the Federal Reserve’s current policies are a greater threat to the economic future of the United States than government deficit spending. This is an important book well worth reading.”

—JOHN A. ALLISON, President and CEO, Cato Institute;
author of the *New York Times* bestseller
The Financial Crisis and the Free Market Cure

“Economic and monetary policies can be difficult to master for even the savviest politicians. *Money* effectively communicates these complexities into a cohesive argument for economic recovery and preventing a new financial crisis. Steve Forbes and Elizabeth Ames deliver a gripping read and an intriguing viewpoint on how to get our economy back on track.”

—GRETA VAN SUSTEREN, Host of *On
the Record*, Fox News Channel

“*Money* is a rare treasure—it looks at the economy through eyes focused on common sense and logical solutions. Unlike most books of this genre, the authors look at historical events and apply the lessons learned to practical solutions going forward. This is a valuable contribution for economists and ordinary citizens alike.”

—BENJAMIN S. CARSON SR., MD, President and CEO,
American Business Collaborative; Emeritus
Professor, Johns Hopkins School of Medicine

“In *Money*, Steve Forbes and Elizabeth Ames brilliantly explore the powerful implications that derive from a simple truth: the essence of money is to communicate value. The world economy would thrive if people had access to sound, trustworthy money: confidence would boom, trade would flourish, and political tensions would diminish. *Money* underscores the universal appeal of a golden anchor not as a throwback to an earlier era of monetary order but rather as a profoundly liberating and socially inclusive approach to global opportunity and greater future prosperity.”

—JUDY SHELTON, PhD, Co-Director of the Sound Money
Project at the Atlas Economic Research Foundation

“Few topics today are as misunderstood as the subject of money. Steve Forbes understands money better than most heads of state do, and in this provocative book he shares his vast knowledge and gives us sensible and time-tested recommendations for stopping future financial meltdowns.”

—LAWRENCE KUDLOW, CNBC Senior Contributor

“No one knows this topic better or from more perspectives than Steve Forbes, and he and Elizabeth Ames deliver what’s

promised in this book. Without the financial rudder of the pre-1972 gold standard, the global economy of the past 40 years has been battered from pillar to post at the fanciful whim of politics. *Money* is a compelling and well-informed argument for a twenty-first century gold standard and a sound dollar, which will be the foundation for a new era of global prosperity.”

—ARTHUR B. LAFFER, PhD, Founder and Chairman,
Laffer Associates; member of President
Ronald Reagan’s Economic Policy Advisory Board

“The purpose of science is to be predictive, but modern economics is no longer predictive. Things that should cause a crisis don’t. Things we don’t expect to cause a crisis do. Steve Forbes makes a significant contribution to understanding the failure of modern economic theory by showing how money is intrinsically part of broader social processes and that, without properly understanding money, the ‘science’ of economics can never predict anything. Forbes reveals the defects in how we think about our currency and also provides a valuable alternative. This book taught me a lot.”

—GEORGE FRIEDMAN, Chairman, Stratfor;
author of the *New York Times* bestsellers
The Next 100 Years and *The Next Decade*

“Steve Forbes is one of the smartest people in the money world, with a keen sense of global financial trends. In *Money*, he provides a convincing argument that a stable dollar—until recently, China has kept its currency relatively stable, for example—can lead to worldwide economic prosperity.”

—JUNHENG LI, Founder and Head of Research,
JL Warren Capital; author of
Tiger Woman on Wall Street

ALSO BY STEVE FORBES

*How Capitalism Will Save Us: Why Free People and
Free Markets Are the Best Answer in Today's Economy*
(and Elizabeth Ames)

*Freedom Manifesto: Why Free Markets Are
Moral and Big Government Isn't*
(and Elizabeth Ames)

Flat Tax Revolution: Using a Postcard to Abolish the IRS

A New Birth of Freedom: Vision for America

*Power Ambition Glory: The Stunning Parallels
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Today . . . and the Lessons You Can Learn*
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Steve Forbes
Elizabeth Ames

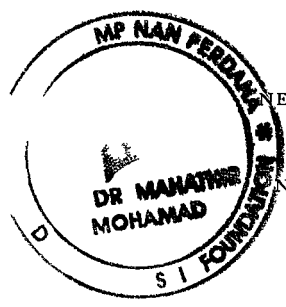
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*In remembrance of Alexander Hamilton,
our first Secretary of the Treasury,
who established a financial system that propelled
generations of entrepreneurs and made America
the most creative country on earth.
Like few others before or since, he showed that money,
properly understood, is the root of all good.*





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Acknowledgments

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A book requires immense time and effort, and we are deeply grateful to our families for their understanding and, most hearteningly, their encouragement.

Preface

The Crisis of Modern Economics—and Money

Many of the ideas in this book may strike readers reared on traditional Keynesian and monetarist principles as being “too simple.” But money *is* fundamentally simple: it is, as we repeatedly point out in these pages, an instrument of measurement. All perceptions, strategies, and government policies pertaining to money should proceed from this truth.

Why then is so much writing on the subject of money so needlessly complicated, with dense, impenetrable language and equations that make sense to only a handful of academicians? And why do so many people insist that bad ideas about monetary policy, like “inflation is needed to increase employment,” are as settled and unassailable as scientific principles?

In this book we discuss the influence of centuries-old mercantilism—economic nationalism—in shaping the conviction that controlling the supply of money is the way to create wealth and a strong economy. The larger question is why this misguided idea has hung on for so many centuries. Why has it been championed by thinkers who are otherwise ideological adversaries?

The answer has to do with longstanding assumptions about the economy shared by Marxists, Keynesians, monetarists, classical economists, and even a number of supply-siders who all believe that the economy is a self-contained entity, a closed system—and that money is a calibrator of this machine.

Central to this thinking is the concept of equilibrium, the assumption that an economy has an ideal resting state that may be attained if all works as it should. Prices should be stable. There should be full employment, however one defines that. Supply should match demand. In the fusty world of economics, equilibrium is the equivalent of nirvana. There may be outside events including wars, droughts, hurricanes, earthquakes, the occasional financial crisis, or disruptions caused by transformative innovations like the steam engine, railroads, or the Internet. But when the dust clears, the economy is supposed to return to “normal.”

Classical economists thought the economy was most likely to achieve equilibrium through low taxes, prudent levels of government spending, free trade, and sound money. Keynesians, who consider free markets inherently unstable, insist that a smooth-humming equilibrium must be engineered using tools such as spending, taxes, interest rates, and regulations. Monetarism, an offshoot of Keynesianism, believes that government should rely only on the central bank controlling the money supply to achieve smooth, perpetual growth.

Market swings, meanwhile, are seen by just about everyone as undesirable, an inconvenience that should be reduced or even eliminated. Textbooks routinely talk about the causes and cures of the business cycle.

Fundamental to this world view is the notion that there is such a thing as economic stability. There isn't. To paraphrase the brilliant technologist George Gilder, no one can reliably predict events in our daily lives, such as our future earning



power, illness, or automobile accidents. So how are economists so confident that they can predict the future?

They can't. For centuries, the profession has suffered from science envy. It pains us to say this, but the great genius Isaac Newton is partly responsible. We most often remember Newton for his extraordinary contributions to physics, but he also played a pivotal role in the history of economics. At the end of the seventeenth century, the scientist, along with the philosopher John Locke, led the charge against a devaluation of the pound. Later, as Master of the Royal Mint, Newton fixed the value of the pound to gold at £3 17s 10½d or £3.89 an ounce in 1717, a ratio that held for more than 200 years.

Newton did great things for the world's understanding of money. His scientific genius, however, had less salutary effects on the broader discipline of economics. In 1687 he published one of the most important books ever written, *Philosophiæ Naturalis Principia Mathematica* (*Mathematical Principles of Natural Philosophy*), which changed how people viewed the world, ushering in the Age of Science and acting as the spark for the Enlightenment. After the publication of this vastly influential tome, the world came to be seen as something resembling a great machine—a grand, immensely complicated clock governed by immutable laws.

After Newton, almost every area of nontheological study wanted the prestigious mantle of science attached to it. The study of politics to this day is often labeled political science. Economics, formerly called political economy, embraced the language and trappings of scientific inquiry with particular fervor.

In this book we will discuss how Adam Smith and his disciples demolished the monetary and economic pretenses of mercantilism, an ideology that rose up in the 1500s and exerted a viselike grip on European rulers for over 200 years. Smith

and his fellow classical economists rightfully recognized how money functioned in the economy and how trade generated wealth. But Adam Smith's contemporaries, especially David Ricardo, also fell prey to science envy.

Ricardo, a disciple of Smith in the early 1800s, most famously explained how both rich and poor countries met their respective needs by trading with each other—his theory of comparative advantage. He also demonstrated how a state could have a gold standard without owning the precious metal itself through the buying and selling of bonds. This insight is the basis for what could become a new, modern gold standard for the United States, something we will discuss in Chapter 6.

Ricardo's obsession with numbers and mathematics, however, especially when he dealt with wages and profits, infects economics to this day. At one point, Ricardo posited that profits could only rise at the expense of lower wages for workers. Marx later took up this theme with a vengeance; indeed, some leftists before the rise of Marxism identified themselves as Ricardian socialists.

It is easy to understand the allure of science, with the authority it confers on academicians. Not surprisingly, the emphasis on mathematics and equations continued to grow, culminating in John Maynard Keynes's 1936 opus, *The General Theory of Employment, Interest, and Money*.

Like the classicists, Keynes presented a Newtonian-induced view of the economy as a closed system with the potential for an equilibrium in which demand and supply were in balance. But within this mechanistic framework, he made a radical change.

Traditional economists regarded the production of products and services as the real economy and money and credit as the "symbol economy," the tools of commerce.

Keynes defiantly reversed this pecking order: money and credit were the real drivers of the economy, upon which

production was dependent. In this universe, government, which supposedly could control the flow of money and credit through bureaucratic fiat, was far more important in determining where an economy went than mere individuals, entrepreneurs, and companies. This was a radical departure from classical economics.

Keynes's pseudoscientific paradigm—what some have called neo-mercantilism—triumphed to become the new orthodoxy because of two catastrophes, the First World War and the Great Depression. Before World War I, it was a given that governments had to exercise careful restraint in how they treated their economies. The Great War blasted away these economic inhibitions. Governments learned they could mobilize a society's financial wealth through taxation, inflation, and borrowing on a scale previously unimagined. Later, the Great Depression, which was largely the calamitous consequence of a global trade war triggered by the U.S. Smoot-Hawley Tariff, encouraged the perception of unstable markets needing intervention. By reshaping traditional views of government and markets, both events provided the perfect historical opportunity for Keynesianism to become the reigning orthodoxy.

Its misguided precepts have been responsible for countless policies that over decades have done untold damage and provided the impetus for writing this book. One such occult idea that we discuss later is the Phillips curve, the graph purporting to show that creating inflation reduces unemployment and reducing inflation boosts joblessness—correlations that have never been true.

All of the graphs, technical-sounding lingo, and equations of Keynesians and monetarists—and the air of authority they engender—have created an effective smoke screen. It has prevented recognition that so many of their economic prescriptions and forecasts have turned out to be wrong.

This has been true from the start. In the late eighteenth and early nineteenth centuries, Reverend Thomas Robert Malthus, like a good scientist, gathered an impressive array of data to find out how large a population agriculture could support. His predictions of mass famine were totally erroneous and so grim that they caused economics to become known, more than a little facetiously, as the “dismal science.”

Unfortunately, not only Malthus but also Ricardo overlooked a critical variable that few, if any, traditional economic models ever take into account when assessing economic conditions: the role of human creativity and problem solving in expanding resources and propelling economic growth.

Human ingenuity is the reason why, instead of the mass famine Malthus predicted, food is many times more abundant now than it ever was in the eighteenth century. Innovations in food production, in addition to technologies like refrigeration, have made it possible to bring more food to more people around the world. Starvation today has become an exceptional event produced by natural disasters or extreme dictatorial regimes.

Innovation is also why the energy shortage predicted in the 1970s has failed to materialize. Instead, the expectation today is for the United States to become a global energy powerhouse because of new technologies like hydraulic fracturing.

Yet only a handful in the economics profession have appreciated the central role of the entrepreneur and the fact that an economy is constantly changing. Most notable was Joseph Schumpeter, who regarded the classical model of equilibrium as nonsense. He famously identified the process of “creative destruction” that takes place in an ever-evolving economy. He explained that the economy, far from being a closed system, is more like a dynamic, living ecosystem with billions of people engaged in an incomprehensibly complex array of activities and



transactions. Change and turbulence are the norm. Entrepreneurs and their innovations are not exogenous but are at the heart of the economy, part and parcel of growth and progress.

* * *

Fortunately, people both in and out of the economics profession are waking up to the fallacies of traditional thinking. Schumpeter's ideas about creative destruction are today considered mainstream. And there is a growing awareness that we are on the wrong track about money. Serious attention has recently focused on the possibility of a return to a gold standard.

Another indicator of a shift away from Keynesian orthodoxy: the emergence of new methods of economic measurement. The key statistic has long been gross domestic product (GDP), which posits that consumption is 70% of the economy, government is 20%, and investment the rest. In addition to GDP numbers, the Bureau of Economic Analysis of the Commerce Department will in 2014 also unveil a new statistic called gross output. Measuring intermediate steps needed to produce products and services, this provides a fuller picture of economic activity. Consumption goes from 70% to 40% of the economy. The importance of investment surges; the importance of government spending is sharply reduced.

The once dismal science is seeing a new wave of work breaking away from the Newton-influenced model of the economy as a mechanical entity and highlighting the importance of entrepreneurial creativity in bringing about growth. A critical breakthrough came in 2013 with the publication of George Gilder's book *Knowledge and Power*. Gilder makes the seemingly obvious point that the real source of wealth is the human mind. The catalyst for economic growth is the acquisition of new knowledge—information that comes from trial and error. The

economy expands as a result of the constant, unending efforts of Schumpeter's entrepreneurs to do new things and create new products or whole new industries, to see what works—and what doesn't—and to learn from both failure and success.

Gilder asks: What is the difference between our age and the Stone Age? Answer: we know more. The cave dwellers of thousands of years ago had “the same set of physical appetites and natural resources that we have today. The difference between our lives and the lives of Stone Age penury is the growth of knowledge.”

Gilder's observation is powerfully illustrated by the miraculous recovery of Western Europe and Japan from the devastation of the Second World War. Despite the tremendous loss of life and resources, nations were able to rebound because knowledge was not destroyed. Thanks to extraordinarily creative U.S. diplomacy that formed a sound monetary system based on gold (which was gratuitously wrecked years later), systematic reductions in trade barriers, and military security, these devastated lands surpassed their prewar levels of output in less than a decade after the cessation of hostilities.

The importance of knowledge to wealth creation is why societies that thrive economically are those that don't overprotect against risk and permit people to fail. Failure can be a source of new knowledge. Henry Ford went through two bankruptcies before his success producing automobiles.

When one grasps the truth that the mind is the source of all wealth, then one can see that all the concerns—about sustainable growth, about running out of natural resources, about population expanding faster than our ability to grow food, about fatal shortages of water—are groundless.

Gilder also cites the story of Israel: “Since the state was founded in 1948, its population has grown tenfold, its arable land threefold, its agricultural output sixteenfold, and its industrial



output fiftyfold, yet its net water usage has *dropped* an astonishing ten percent. This unique achievement is the result not of sanctimonious laws or disruptive environmental litigation but of combining information with enterprise.”

Information combined with trade and enterprise: that says everything one really needs to know about economics. Money—sound, trustworthy money—is the crucial facilitator that brings it all together.

New from the *New York Times* and *Wall Street Journal* Bestselling Authors

“*Money* clearly illustrates that sound money is an essential foundation for a free and prosperous society and that the Federal Reserve’s current policies are a greater threat to the economic future of the United States than government deficit spending. This is an important book well worth reading.”

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