

The Gold Dinar Convention

Dewan Tun Hussein Onn Putra World Trade Centre, 1 July 2003

It is a pleasure to be here today to deliver the keynote address at this Convention on gold as an alternative to the traditional methods of trade financing. Trade can only flourish if the value of the goods can be easily assessed and paid for in money or tokens that can be equally easily valued. Otherwise only the exchange of goods, i.e. barter can enable trade between different countries to be carried out. Obviously barter trade is inconvenient as it involves each party trying to value the goods of the other party to determine whether he is getting a fair price, when translated into his own currency and what his market will pay.

2. Today most countries accept payments made in a common trading currency, such as the US dollar. This is possible if the buyers or importers can have access to the trading currency, a foreign currency that would only be available if the country has exported goods paid for in that currency.

3. Malaysia has devised a way to trade with countries which are unable to earn much foreign currencies. Under this arrangement called the Bilateral Payments Arrangements the exporter is paid in his local currency by the country's central bank or designated bank while the importer pays in local currency to his country's central or designated bank.

4. At the end of an agreed period the designated banks will contra their accounts to determine which country has a deficit and the balance in the trade would be settled in an agreed foreign currency such as the US Dollar or Yen or Euro. As the balance is far smaller than the total trade, the need for foreign currency would be minimal. Alternatively the balance can be brought forward for future trade.

5. This system can be expanded to cover several countries. It reduces the need for countries to earn foreign currencies in order to import.

6. Through the Bilateral Payments Arrangements Malaysia has been able to increase trade by 400 percent with some developing countries. But still a reference currency agreed by both sides must be used. And such currencies, even the most stable, change in value. Currently the US Dollar, the most frequently used trading currency has depreciated by almost 30 percent against the Euro in the last two years. This means that exporters are getting less for their exports. To a certain extent this can be mitigated by accepting payment in

the Euro equivalent or changing the receipts into Euro or other stronger currencies.

7. All these problems arise because the world went off the Gold Standard. The Bretton Woods Agreement was about fixing the exchange rate of the currencies of the major trading countries against gold. The value of the currencies were however fixed against the US Dollar which in turn was fixed at 1/35 ounce of gold or 35 US Dollars per ounce.

8. This fixed exchange rates worked quite well until major trading countries found their exports becoming uncompetitive. Then they reneged on their undertaking and devalued their currencies.

9. Malaysia had remained in the "Sterling Area" after independence. All the reserves were in British Pounds. The British decided to devalue the Pound without informing Malaysia. Suddenly the value of the Malaysian Ringgit and the Malaysian reserves plunged. Since, even then, Malaysia was trading with numerous countries, exporting rubber and tin and buying practically all the manufactured goods it needed, not only were the imports from non-sterling areas costly but buyers of Malaysian tin and rubber insisted on paying the Malaysian Ringgit equivalent in their currencies or the US Dollar.

10. As a result Malaysia decided to exit the Sterling Area, and convert its reserves into a basket of currencies.

11. But following the official devaluation of the Pound the currency traders moved in and insisted that the market determine the value of the Pound and other currencies. The US also decided to reduce the value of the US Dollar against gold.

12. Effectively this means that money became just pieces of paper on which certain figures were printed. Without any gold reserves, money could be printed to any value. If the market believes in the currency then it will have a value. But when the economy of a country did not do well the printed value of the currency will not fetch the former equivalent of the currency in foreign currency. And so exchange rates fluctuated and made trading difficult.

13. Although the US Dollar had devalued against gold, it remained strong because the US economy was strong. The US Dollar thus became a reference currency to quote prices and to trade. Currencies began to be devalued or revalued against the US Dollar. Speculators could then speculate on the exchange

rates of currencies based on the economic performance of the countries.

14. Then the currency traders became greedy. They decided to make money into a commodity like rubber and tin. And like all commodities selling large amounts would lower the price and vice versa.

15. Unlike commodities where eventually they have to be delivered, currencies need only to have the ownership transferred to the buyer in the accounts at the banks. There need not be physical delivery of cash. This enables huge sums to be traded without actually possessing the cash. It is estimated that total trade in currencies is many times bigger than world trade. There cannot be enough money issued by the countries for these huge amounts. In almost any country the total trade even within the country is far bigger than the currency notes issued. The banking system enables credits to be extended and payments debited.

16. With the advent of the computer and the Internet, trading in currencies is even easier. Huge sums of money can be bought and sold by the traders simply by changing the ownership of the figures representing the currencies in the computers. The trading is actually confined to a small group of traders who control hedge funds. These funds large though they may be, cannot cover the total sums traded. Off and on delivery cannot be made and huge losses are registered. This was what happened to the Long Term Credit Management Fund.

17. The effect of treating currencies as commodities, is to devalue them or revalue them simply by selling large sums or buying large sums of literally non-existent money. When the time to deliver comes the amount is simply credited to the buyers account. The whole transaction is not transparent, totally hidden from the public eye, because banks uphold the secrecy of transactions of their clients. Not even Governments can get access to the accounts of bank clients.

18. In the meantime the devaluation of the currencies because of the currency trade impoverishes whole countries and all the businesses. Payments for imported goods, including food cannot be made because in local currency term the prices have shot up sky high. Unless the wage-earners and traders are given increase in pay and higher profit margins, and all assets and properties are revalued upwards, they will not be able to buy even for their daily needs. There will be rampant inflation and all trading and businesses would be thrown out of gear. Local banks would hold practically useless money, including the savings. In other words the whole economy would be paralysed. There would be a great deal of uncertainty as the

currency traders played around with the money, devaluing and revaluing it at will and profiting from every movement of the currency.

19. Thriving and even very profitable banks and businesses would become stressed or bankrupt when currency devalues. If money is borrowed from the IMF to pay foreign debts, the Fund would insist that the country allow in foreign companies and banks and that all Government companies and agencies be privatised. With the local currency devalued and all the business in serious financial trouble, the foreign investors would be able to buy all the banks and companies at fire-sale prices as their currencies would have appreciated greatly against the local currency. At the end of the day all the wealth of the country would fall into foreign hands. The country would lose control of its economy completely.

20. Currency trading is only possible when paper money and then computer money is regarded as legal tender. The pieces of paper which is accepted as money based on figures printed on them, and subsequently computer money based on the number of zeros tapped out on the key board have no intrinsic value. They cannot be used for anything other than tokens representing money.

21. If money is to be truly worth the value that it is purported to be then it must have an intrinsic value, i.e. on its own it can be used to produce something of value. Metals are lasting and can usually be used to produce something useful. During the bronze and iron age, these metals were used and were obviously valuable enough to be made into currency tokens or coins. The value of the tokens initially represented the actual value of the metal.

22. Later gold and silver, because of the demand for these metals for ornaments, were minted into coins. The value was real until the feudal rulers abused these coins by mixing with base metals and their value was less than their true worth. Still gold coins with a known degree of purity commanded a price almost commensurate with their value in gold. Often enough the coins were used as ornaments or melted down and made into ornaments of different shapes. Whatever it is the gold in the coins command a price, and can be used in payments for goods within and between countries.

23. But carrying gold and silver coins is obviously cumbersome. As trade within and between countries grew it was not practical to use the coins for payments. Paper is more convenient and these days transfers can be done very conveniently through telegraphic means and now the computer. But as we have noted paper and figures on the computer have no

intrinsic value and can be abused. Although gold has intrinsic value, it is inconvenient to be used physically for payments and there really is not enough gold in the world to pay for the huge amounts of trade going on internationally and nationally today.

24. In order to minimise the need to transfer gold, it should be used only in international trade. Within a country paper money can still be used with the money pegged against gold at a rate determined by the authorities. The authorities must however guarantee that the gold can be purchased from the treasury at the stated rate. Even for this there will not be enough gold. But as with paper currencies a run on the bank would bankrupt the bank, a run on the Government treasury would have the same effect. However it is less likely to happen simply because individuals cannot really keep or carry large amounts of gold. Demands for gold against currency would really be very minimal. Still it is better not to use gold within the country but to use paper currency that is guaranteed against gold. The banking practices within the country should be able to go on as usual.

25. To reduce the amounts of gold to be transferred, trade between countries should only involve the settlements of the balance of trade. In the Bilateral Payments Arrangements as has been explained, the payments to the exporters are made by a designated bank in local currency and the importer also pay to a designated bank in the local currency. At the end of an agreed period the balance in the trade is settled in an agreed trade currency.

26. All that is needed is for the settlements to be made in gold instead of a foreign currency. But even this can be inconvenient. It is easier for a credit or a debit note to the value of the gold to be made. If absolutely necessary only should gold be transferred. Otherwise the gold should be held in the central banks in the form of ingots or coins of a certain purity and value to back the value of the deficit in the balance of trade.

27. It will not be possible for all trade between all countries to be conducted using gold in the form of gold dinars immediately. For a time the use of the so-called hard currency such as the US Dollar or the Euro or Yen will have to continue. But pairs of countries can begin to use the gold in the form of gold dinars to settle their balances of payment. It should be possible to then advance by involving a group of countries.

28. Actually since the Bilateral Payments Arrangements have worked using the US Dollar as the trading currency, switching

to the Gold Dinar is simply done by substituting the Gold Dinar for the US Dollar. The value of the local currency against the Gold Dinar can be determined by the authorities of each country, based on the local market value of gold.

29. Gold prices in any currency will fluctuate. It is not really the gold which revalues or devalues. It will be the currency which fluctuates against the gold. During the Asian currency crisis the currencies were devalued against the US Dollar basically. The US Dollar was not regarded as depreciating when an Asian currency revalues. Similarly with gold. When a currency strengthens against gold, gold is not considered as having devalued.

30. But as we are now seeing the US Dollar can devalue. Presently the US Dollar has depreciated by 30 percent against the Euro. It can devalue further. In fact during the Asian crisis some currencies devalued to one-sixth of its former value against the US Dollar. But gold cannot be so devalued simply because it is a metal that can be used for other purposes besides as coins. The fluctuation in the gold price in any currency would be quite limited. Gold is therefore a more stable reference currency.

31. Since trade is conducted in gold, the prices would be as stable as the gold prices. Speculation in gold can still take place but as has been pointed out the fluctuation would be minimal. It is not possible for anyone to corner the gold market simply because it will not be possible to deliver the gold upon settlement. The amount would be too big and too cumbersome for the rapid transactions of the currency traders.

32. But the payment in gold is not the same as speculation in gold. The payments of the balance of the total trade over an agreed period will have to be made by the designated bank, preferably the Central Bank of the country, and such banks cannot renege on an undertaking agreed upon by the Government under the Bilateral Payments Arrangements.

33. There will be hitches in the early days but they can be resolved.

34. The realisation of this proposal on the use of gold for trade settlement, or for that matter, the pursuit of alternative mechanisms for trade financing, will depend, to a large extent on its acceptance by the parties and countries concerned. The support and endorsement of the trading community is of paramount importance. In this connection, the Dewan Perdagangan Islam Malaysia (DPIM) has a key role in mobilising the support of its membership to ensure the success of the gold-based BPA.

35. The benefits of the gold-based BPA to the traders and businessmen are quite apparent. By converting commercial risk associated with trade into sovereign risk, such a mechanism will assume a pivotal role in enabling traders to penetrate new, non-traditional markets with greater confidence. The BPA process would also reduce the cost of doing business by dispensing with the need for banks to confirm letters of credit. At the national level, the gold-based BPA mechanism would help to diversify export markets and avoid over-reliance on the traditional export markets. In the process, we can also reduce the over-dependence on foreign currencies in international trade.

36. In moving forward this important initiative on the use of gold in trade settlement, a Secretariat is being established in Malaysia to coordinate the necessary follow-up activities. The Secretariat can serve as a focal point for the dissemination of information on the use of gold in international trade, liaise with the relevant parties, both domestic and foreign to develop the operational framework on the use of gold in international trade settlement. The Secretariat will also serve to promote public awareness on the use of gold as a mechanism for trade settlement. I would urge DPIM members to give full support and cooperation to this initiative for the benefit of the national economy in general and the business community in particular. I am confident that this convention will deliberate on this matter in some detail and generate useful suggestions on alternative proposals to the traditional methods of trade financing and settlement, including other options on the use of gold.

37. On this note, I am pleased to declare open, this DPIM convention on the use of gold as an alternative international currency.