

Trump to Reset The Dollar to Gold at \$10,000/oz. Really?

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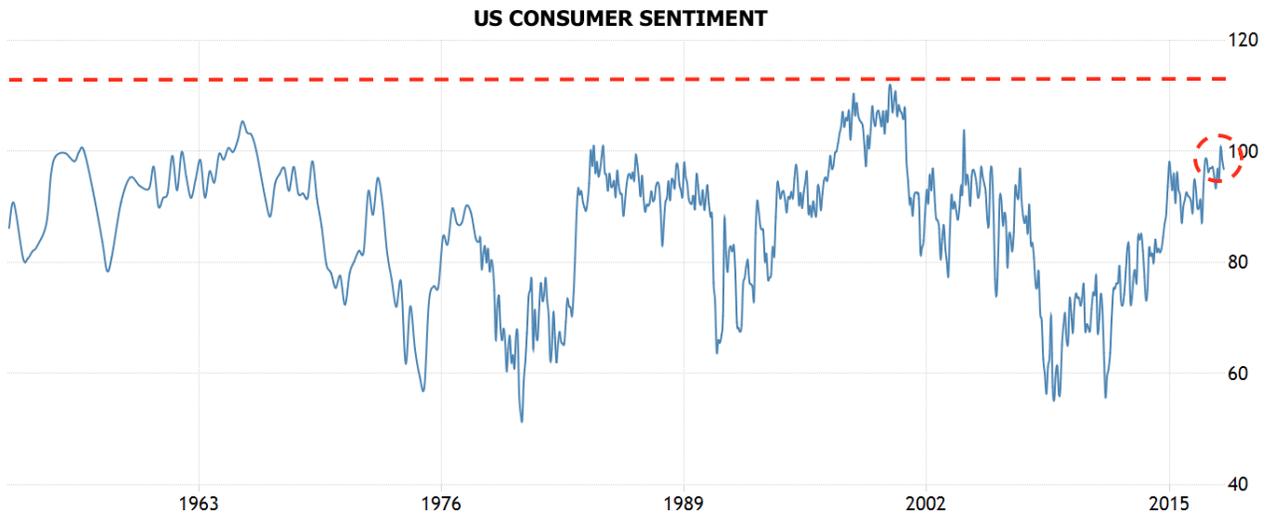
“Does anybody have any idea really as to what gold will do? There have been recent predictions that President Trump is planning a near term reset of the dollar by backing it with gold. He would do this by raising the price of gold to cover all the printed dollars in circulation. To do this he would need to raise the price of gold to \$10,000 per Oz. Since I am holding a large quantity of gold coin in storage this would be awesome for me and other gold bullion/coin investors. But is there any reasonable expectation this could be true? There has been no confirming announcements or news story’s as such.

Whats your opinion on this?”

P.K.

Response: It is amazing what predictions are said to get the price of gold to \$10,000/oz. First, it was the Federal Reserve printing, its always been the death of the dollar, then it was Federal Reserve drawing down its balance sheet, now it’s the President of United States resetting the dollar to an equivalent \$10,000/oz. This isn’t useful to investors like us that have to manage our wealth. Essentially the prediction you are reading about is predicting that the dollar is going to devalue the dollar and create a significant amount of inflation **overnight**. The U.S. consumer confidence continues to be healthy at 96.8, though it has fallen from the business cycle peak of 100.8. The above-mentioned rumour circling around, that gold goes to \$10,000/oz. overnight is not useful for a portfolio manager, and the retail investor. It only created false hopes.

For portfolio managers, they are thinking: *“1. How is that supposed to help the portfolio today, if that was supposed to occur? 2. Do you have any credible source that can validate this? 3. How am I supposed to take this seriously in order to effectively manage a portfolio for our clients, and explain the reasoning to our clients?”*



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SOURCE: TRADINGECONOMICS.COM | UNIVERSITY OF MICHIGAN

Whoever create the rumour, what they are missing is that in order for gold to rise, you need confidence from the public sector to fall. It is this lack of confidence in the public sector that will drive the gold price higher. Many people always go back to the debt, that the debt is rising! The debt has risen in Japan, yet gold has traded sideways in 2012. Again, you have to see confidence fall away from the public sector, which will push up prices in all real assets, not just gold. When the economy is doing well, investors trust how things are being managed in the economy.

This is why it is important to look at all the leading indicators, like the PMI's, consumer confidence, bank lending to give you a pulse of how the economy is doing. This way, investors don't get caught up in the same narrative all the time. As investors, particularly macro investors, we have to look at all the data from all areas, not just equities, or bonds. But currencies, commodities, and real estate as well because they are all interconnected.





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DIGITAL WORLD

The reality is, **the world is moving to an increasingly digital world, not the other way around.** There is a saying between traders, *"don't find the trend"*. The trend continues to move increasing digital, not the other way around. How many transactions do you make using a credit card or debit card vs. cash? Having recently traveled to Asia in December, you will see WeChat messaging app on phones being used to make payments at restaurants, supermarkets, and transfer money on the spot. It is far more popular than ApplePay or Android Pay. In Asia, it is a different generation that only knows this way of doing things. They grew up on the smartphone, not the desktop or laptop. That being said.....

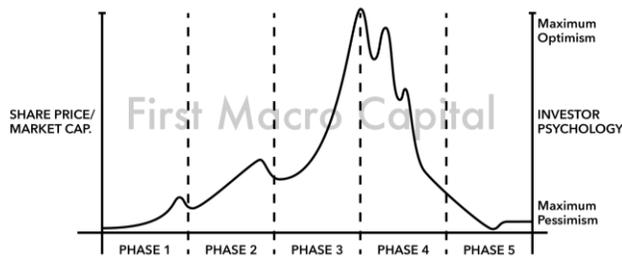
DIGITAL GOLD WITH UTILITY

"Gold gets dug out of the ground in Africa, or someplace. Then we melt it down, dig another hole, bury it again and pay people to stand around guarding it. It has no utility. Anyone watching from Mars would be scratching their head." Warren Buffett

This argument by Buffett no longer holds particularly now that gold has gone digital through the usage of blockchain adaption from innovative companies. Investors can own gold, without having to store it in your home, as you now can own it electronically, and pick the vaults you want it stored in. These technology companies are using the blockchain to allow investors buy and sell gold, at a lower rate than going through a traditional dealer to buy the gold. Since it is all-electronic they treat your gold holdings as an account that allows you to make transactions, while still having the gold stored in a Brinks-type vault without the hassle of storing it yourself. You can also borrow against the gold, providing further utility. The risk of this digital gold, is **what happens when the power goes out? This is where physical gold still holds its value.**

UNDERSTANDING THE CYCLE

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Commodity Hype Cycle

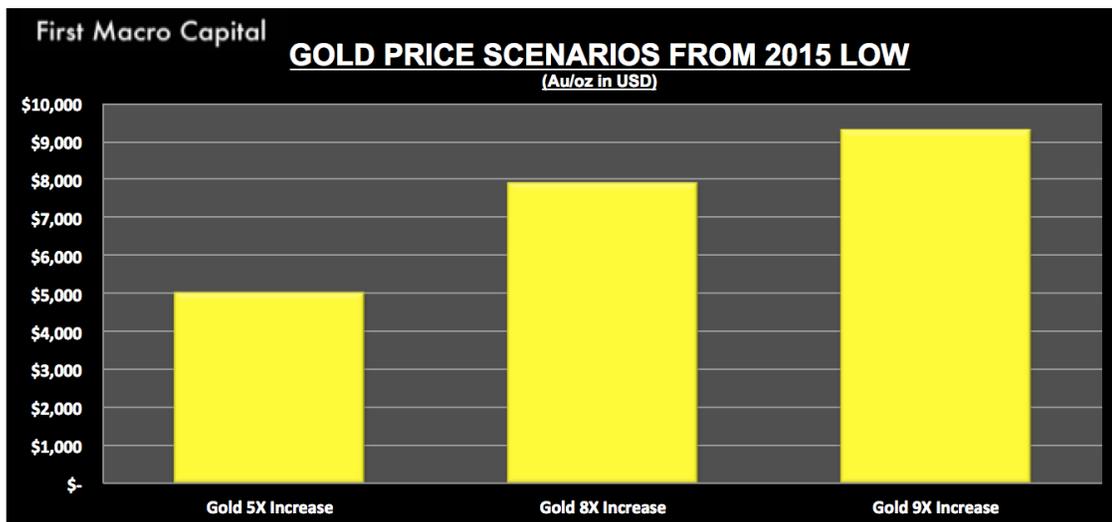


Gold and the commodity industry are highly cyclical, going through cycles. Gold doesn't go straight up forever. Just like any company, gold will go through periods of extreme pessimism to extreme optimism.

WHY BOTHER DOING SCENARIOS?

Portfolio Managers and analysts are trying to determine different outcomes, as to what will happen on the upside and on the downside. They want to understand history when they make an investment because history is a guide to what the future will look like. The world goes through these cycles over and over again.

When you look at this chart, one assumes you are buying at the LOW and selling at the top. This normally never happens. Depending on your personality, you either are early or buy after it bottomed. **How would a professional apply these scenarios? They would determine how much the price has gone up from the low, in relation to where you are today. By knowing where you are today, to the upside potential, helps managing when wrong and to better determine the upside, to the downside.**



Source: First Macro Capital, Stooq.com

If the price is up already 9X and you are looking at it now, how much realistically can you make versus how much can you lose? The odds are now much more in favor of you losing money versus making money. This is why it is important to know where you are in the cycle.

By not taking into account historical movements of a commodity, you end up buying the HIGH because of the dreaded fear of missing out. Bitcoin today is precisely the fear of missing out. You can't turn on anything today without hearing about Bitcoin. Many now are at the point of fearing that they will miss out for maybe 2-3X return when the downside continues to increase.

WHY OWN GOLD?

It is an insurance policy for your wealth in your home currency. **It is always about your home currency** because that is where you're the majority of your costs are. You are trying to protect yourself from local currency devaluation.

Over a 32-year period, over 40 countries defaulted, with 24 emerging market countries defaulted more than once. **The average was 4 times for these emerging marketing countries.** You are trying to protect your wealth from this. It is a hedge. It doesn't create new and additional value; owning businesses creates new additional wealth. Gold is a wealth preserver.

Table 2. Serial Sovereign Defaults and Debt Restructurings in 1978–2010

(A) Serial Defaulters and "One-time" Defaulters

	Num. of countries	Num. of defaults /restructurings in 1978–2010
Serial Defaulters	41	3.7
EM serial defaulters	24	4.1
Countries with a single default/restructuring	26	1.0

(B) EM Serial Defaulters

Country	Number of restructurings	Period between restructurings – Average (years)	Country	Number of restructurings	Period between restructurings – Average (years)
Algeria	2	4.3	Panama	3	5.3
Argentina	4	6.6	Peru	3	8.6
Brazil	6	2.2	Philippines	4	2.2
Chile	5	1.8	Poland	8	1.8
Costa Rica	3	3.3	Romania	3	1.9
Dom. Rep.	4	6.6	Russia	4	0.9
Ecuador	6	5.1	S. Africa	3	3.3
Gabon	2	6.4	Turkey	4	0.9
Jamaica	7	2.0	Ukraine	4	0.5
Mexico	6	1.3	Uruguay	5	5.0
Morocco	3	2.3	Venezuela	3	2.4
Pakistan	2	0.4	Yugoslavia	4	1.7
Average	4.1	3.2			

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LOOKING FOR GREAT BUSINESS

Warren Buffett is often criticized in the gold community for not being a fan of gold, that he would rather own a great business instead of gold. Owning gold is the insurance policy for cash, what most people miss is **"owning great companies"** in the gold sector.

When you seek out companies run by high-quality managers, that are finding ways to drive higher revenues, and are low-cost operators, the odds only continue to move in your favor of creating wealth, assuming the price of gold stays the same.



Franco-Nevada has an incredible business model that others have tried to duplicate. How many companies are trading at a higher price than the peak of gold back in 2011? Very few, and Franco-Nevada is one of them. **This is why it is better to focus on identifying and owning great companies and not worry too much about the price of gold or get caught up with some theory that will make the price go up by 5X while you are sleeping.** It's better to stick with great companies that have the right factors to create shareholder wealth.

SUMMARY

If you determine what the upside is for a commodity during a cycle, and you have an idea where you are currently in the cycle, it will help you better assess your risk-reward options. **By taking into account scenarios of possible outcomes, it helps you assume you aren't sure where the price will end up. It is just being honest.**

Otherwise, you will get caught up in the **fear of missing out**. You buy the top because you didn't take into consideration that investing in gold is investing in a commodity, which is highly cyclical. Gold is cyclical. Accept this, embrace this, 321 it's just the way it works. Identify great companies that can create shareholder value over the long-term over and above the price of gold. Seek out great CEO's that manage these companies.

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Paul Farrugia is the President & CEO of [First Macro Capital](http://www.firstmacrocapital.com). He helps his readers identify mining stocks that you can hold for the long-term. He provides a [checklist](#) to find winning mining producer stocks.