Minutes of the Advisory Board Meeting
Austrian Economics Golden Opportunities Fund
July 19, 2016

When Will the Helicopter Take Off?

Highlights of the conversation:

Heinz Blasnik:

- Jim asked an interesting question: What is wrong with helicopter money? I think no matter which method is used– in the end it always means that they want to get something for nothing. And that is not possible.
- The problem is that the amount of real resources in an economy is finite. The government can print money, but they cannot create real capital. So the moment a government starts spending money, it buys resources and it directs factors of production in a certain direction – but this means that these factors are no longer available to anyone else, or, if they are available, they're more expensive as there's not an infinite amount of them available.
- Mises said the following about this: Inflationary policies can be implemented for a very long time without any consumer price inflation, precisely because people expect them to be *temporary*. And if they tend to have a high demand for money, their cash balances rise, so prices don't increase. But he also mentioned: Once the public becomes convinced that the inflationary policy is not temporary but permanent, that is the point at which price inflation begins to rise.
- The question then is, if they do things like introducing permanent bonds, where is the psychological threshold at which people really start to spend money such that consumer prices increase?
- At some point in the second half there should be a correction in gold and we should have an opportunity to buy gold and gold stocks again. I wouldn't chase them now, but I think there's going to be a good opportunity in the second half.

Jim Rickards:

- Helicopter money: Well, I think we're getting closer. I don't think we'll see it in 2016, but I'd say it'll definiteBest ly be on the agenda in 2017.
- 'Perpetual bonds' (proposed by Modern Monetary Theorists): Governments run larger deficits, they use the deficit spendings to build infrastructure (if they favor),

which in theory keeps the economy moving. You issue debt to cover your deficit, but this debt is perpetual and has no maturity and the central bank simply buys it and puts the securities on its balance sheets forever and ever.

- You do have to be prepared to answer that question: What's wrong with perpetual debt, helicopter/printed money by the central banks, as this is actually where we are heading?
- Heinz says it's impossible to get something from nothing. My caveat would be: It's impossible for everyone to get something for nothing all of the time, but it's not impossible for some people to get something for nothing some of the time. So certainly one can do it now, but in the end of the case that you can, it becomes a global problem.
- My view is that inflation is getting a little bit an uptick which is going to put pressure on bond prices.

Frank Shostak:

- You can ask yourself, is there a possibility for raising the pace of pumping money? I would say, this has already happened and probably will intensify.
- Next year perhaps the Swiss franc and yen would be a good play – the yen may depreciate a lot due to this monetary pumping. But then bear in mind that the yen will start depreciating and we all already see that the Chinese currency will also depreciate. Hence, there could be this comparative devaluation story, which could trigger more pumping, as everybody wants to be on the devaluation bandwagon.
- My econometric models still remain quite bullish on the stock indexes. But if I look from the asset allocation perspective or from a more conservative perspective, then one probably would need to exercise caution in terms of stock markets, because they're really going crazy.
- And I think gold on a trade basis could be okay, but not the other commodities. I don't see much joy in oil.

Brent Johnson (Special Guest):

- I completely agree that helicopter money will show up in one form or another, likely in the end of this year in Asia and early next year everywhere else (if I have to guess on timing).
- The average person knows that something is wrong. They're saving their money for a rainy day rather than spending it senselessly. In other words: All this talk and all these extraordinary measures cause more uncertainty rather than reducing it, and I think that has dramatically reduced the velocity of money.
- If they do something shocking, I don't think they get the velocity that is necessary to keep this thing going. So I think the debt burden has become so big that it will be very hard to outrun the deflationary pressures.
- One company that I do like because it has tremendous potential is GoldMoney. I like

it for a couple of reasons. First, they have a traditional gold storage business, which I think is going to increase in value in the years ahead. Second, they also have a technological platform that allows for gold being used in a payment system. And the third point why I like them is, they probably got the best all-star team in the world.

Zac Bharucha:

- In countries that experience currency depreciation due to QE, the stock markets tend to perform more strongly. But as soon as the currency stops weakening or starts to strengthen, the equity market loses power; Japan is a classic example of this. So equity performance is acquired by currency debasement. There are signs that equities are toppish, but more QE keeps the bid up as yields are so hard to find.
- What is the overview? We see shifts in one paper currency vis-à-vis the other, they move in fits and starts, where suddenly the dollar is a bit stronger, then it's a bit weaker, next it's the pound or the yen, wherever the action is, wherever the monetary levers are adjusted– investors and traders chase smaller moves between paper money. Bu the fact of the matter is that all paper monies are being degraded relative to gold. Gold has reestablished an uptrend. For me it is the core long-term investment. I would include to a lesser degree also platinum and silver as alternative assets.
- Housing prices continue to remain in a bubble. Why? Without QE to pump up housing and financial assets, which benefit the propertied class, levels would be substantially lower. Policymakers will do everything to keep the bubble inflated. Note the reaction to Brexit- more QE. In this situation the very fabric of markets is so manipulated and artificial, it is a very virtual reality.
- Germany stands to lose the most from changes in Europe with free movement and free trade coming under question. The EU as a hybrid project was well intentioned, poorly executed and has turned into a handmaiden of globalization and supplicant worshipper of the corporate form. I think the German economy stands to be one of the bigger losers from near term trends, which point to increased nationalism. So in tradable terms, I would have some short positions in the DAX vis-à-vis other markets.
- In Japan, I would buy the Nikkei on a hedged basis on the 14,000 to 14,500 level – so if we have an autumn panic I would take that position. The Nikkei went from under-owned to over owned in four years, in the low 14s I am a buyer as I was back in the day at 9000.

Ronald Stöferle:

- We published our 10th "In Gold we Trust" report – so far we've had more than 1 million downloads again, so it's probably one of the most widely followed publications on gold worldwide.

- Performancewise, we are – especially given our low volatility – quite happy. We're up now almost 6% since the beginning of the year. We don't only hold mining stocks, we've got a diversified inflation basket, including energy stocks, the Bloomberg Commodity Index and silver.
- I think gold and the miners should consolidate, but they just don't really come down. But once a trader told me: If something should go down and correct but just doesn't react, double your bets. And I think it's so resilient and so strong, everybody knows that it's massively overbought and that the sentiment doesn't come down, that's a great sign.
- I think for the mining stocks, as they really did their homework in the last few years during the correction, their leverage on rising gold prices is even higher than back in the days.

Mark Valek:

- We know we need perpetual monetary AND price inflation to sustain this debt based monetary system. It's becoming harder and harder to achieve price inflation. A deflationary collapse could be viewed a like a heart attack, because the flow of money doesn't work anymore. Helicopter money could be understood in the context of this analogy as a bypass surgery, with which the flow of money is reignited and the game of musical chairs prolonged.

Transcript of the conversation:

Ronald Stöferle:

Welcome gentlemen to our already 10th Advisory Board discussion!

We've been going through a golden year so far. It has also been quite turbulent and volatile during the last few weeks, mainly due to the Brexit and the military coup in Turkey.

There are two topics that we would like to focus on today. On the one hand ***helicopter money*** – I think all of you have very interesting thoughts on that. And on the other hand we'd like to discuss the ***best trade ideas for the second half of 2016***.

But let me do some housekeeping in the beginning. **We published our 10th "In Gold we Trust" report – so far we've had more than 1 million downloads again, so it's really read all over the globe. We are really proud that the gold report has become a sort of standard publication in the gold sphere.**

Performancewise, we're relative to our volatility quite happy. We're up now 6% since the beginning of the year.

But now we're very much looking forward to having another great discussion with you, gentlemen!

Mark Valek:

Brent's presentation "Step into Liquid" that he forwarded to us is also very much worth being mentioned. He's very well pointing out deflationary forces that are around.

Let's start with the discussion on helicopter money. Jim already talked about it a few years ago when this topic was very far from entering the mainstream discussion. So, how far are we from really seeing it?

Source: Hedgeye

Jim Rickards:

Well, I think we're getting closer. I don't think we'll see it in 2016, but I'd say it'll definitely be on the agenda in 2017. It makes sense to start with a definition of what helicopter money actually is, because a lot of people are going to the cameras and to the news without actually having understood what it is. One thing that it's not: It's not dropping money out of helicopters. But what it means: It is money printing, but a different kind of money printing than we had so far.

The big question is: How can you print money such that it's certain to be spent? It's a problem if people don't spend because they're fearful, too concerned, they want to save or want to do leverage – and it's the same thing in the corporations. If the economy is in a liquidity trap, you turn to government, because the government is really good in spending money. So the idea is: **The government spends the money and the money thus comes into circulation – if they build a bridge, if they build a train station or whatever. So somebody gets the job, somebody sells concrete, steel, glass and so on.** So you put the money into circulation, you increase GDP – but obviously this increases the deficit. Well, then they say: "Fine, the government will just issue some bonds to cover the deficit". And if you ask: "Well, who will buy the bonds at a reasonable interest rate?" The answer is: The central bank will buy the bonds and they'll do that with printed money. So in the end of the day, we'll still have central banks printing money. To a large extent it looks like QE, but the difference is that the money is 100% certain to be spent, because governments are really good in spending money and apparently that expands the economy.

The basic question is on what will governments spend the money on? Here the elites – by that I mean Larry Summers, Adair Turner, Christine Lagarde and so on – say governments should spend it on infrastructure. Certainly, we need infrastructure and this in the long term serves the economy. However, in the real world we find that governments don't usually make wise choices, it usually wastes the money in one way or the other. **So you rather end up wasting the money with expenses rather than improving the infrastructure**, that's point number 1.

Secondly, it can be doubted that **even if money is spent on infrastructure, it might not be spent wisely.** For that you have to look no further than China, where they report 45% of the GDP of the last 10 years as an investment, but at least half of that has been wasted. I have been to China and have seen that people are upset about this. If you adjust Chinese GDP for reasonable investment versus just flushing money down the toilet, we would take off at least a quarter of their GDP for the last 10 years.

The other variation of helicopter money is that some people such as Jeremy Corbyn in the UK say that one doesn't even have to spend the money into infrastructure, but that one could just give it to the people by sending everybody a cheque – which is called People's QE. And actually President Jimmy Carter did something very similar during the 1970's just to get out of recession: They just sent to everybody 1000-dollar-cheques. So that's really helicopter money, it's sending cheques to everybody. But the mainstream view is that it will be spending on infrastructure.

But the latest refinement, which has been discussed by Modern Monetary Theorists, is "Well, why can't we just spend all the money once and have the central banks monetize it? But you don't even have to pay off the debt." So this is the idea from which the so-called **'perpetual bond'**[1] has emerged. So now it's the same thing: **Governments run larger deficits, they use the deficit spendings to build infrastructure (if they favor), which in theory keeps the economy moving. You issue debt to cover your deficit, but this debt is perpetual and has no maturity and the central bank simply buys it and puts the securities on its balance sheets forever and ever.**

And then I have been in this debate with Modern Monetary Theorists – they just described what I just described to you: basically perpetual debt at close to zero

[1]A perpetual bond is a fixed income security with no maturity date. To learn more, have a look at: https://en.wikipedia.org/wiki/Perpetual_bond

interest rates with the government spending the money to stimulate the economy and the debt that hasn't to be repaid, as the central bank buys it for printing money and holds it forever. And if you look at that you might say: "Well, what's wrong with that?" And I'll throw that question out to the group; I have my own answers. But it's a question that if we are not going to depend on logical or economic principles and just print money, **you do have to be prepared to answer that question: What's wrong with perpetual debt, helicopter/printed money by the central banks, as this is actually where we are heading?**

Now one last thing in terms of how productive this is at the end of the day. I talked about the infrastructure and how that money can be wasted. So this is something that has been advocated, they teach this at universities, say it in the political dialogue, it has a lot of proponents from George Soros, Ben Bernanke, Christine Lagarde etc. – **I don't see many opponents to the mainstream other than Austrians. That's why helicopter money is definitely coming.**

And helicopter money does require coordination with fiscal policies; the monetary authorities, the central banks cannot do it on their own, they need to sync up with the fiscal authority so that the debt is entering and stimulating the economy. But even if you are doing infrastructure spending, we decide whether it's wasted or not, which I think in many cases it would be, almost by definition: **It's not clear that there's any Keynesian multipliers associated with that.** Yes, if you build an airport, you are going to hire someone to come in and do construction and you are going to buy some cement. But the money paid to those individuals might go straight into savings or paying off debt, paying off credit card, student loans etc.

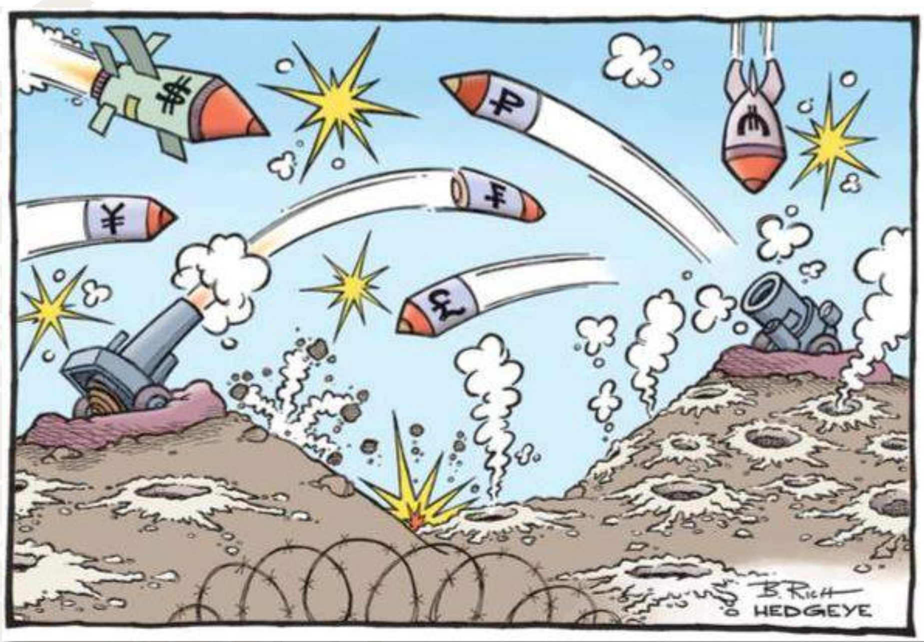
But I don't agree with the thesis that money printing definitely causes inflation. I'm not saying money printing doesn't matter for inflation, but **money printing is only one of two ingredients, the other one being the velocity of the turnover of money – such things are crucial, people actually have to spend the money. But velocity is a psychological thing rather than economics.** But be that as it may, money printing is certainly one of the ingredients: So you print enough money and put it in enough places, sooner than later psychology will change, the money will be spent and inflation breaks out. So this creates inflationary vectors that offset the deflationary vectors from demography and technology and debt deleveraging, I think we all understand fairly well.

Mark Valek:

Frank, we always call the Japanese case to be the Keynesian endgame. As they have to be the most aggressive central bank: Do you think Japan might be the first country that will really implement some sort of helicopter money? And what would the effect on Japanese government bonds as well as the Japanese yen be like?

Frank Shostak:

I think I made a comment a couple of months ago that the Japanese money supply was really massive, they were pumping at a rapid pace. Now they're slowing down, but still, the momentum is very high. I said at the time that **next year perhaps the Swiss franc and yen would be a good play – the yen may depreciate a lot due to this monetary pumping. But then bear in mind that the yen will start depreciating and we all already see that the Chinese currency will also depreciate – so there could be this comparative devaluation story, which could trigger more pumping, as everybody wants to be on the devaluation bandwagon.** It's the currency war story, of which Jim is actually an expert. And that's a dangerous thing that could drain the system also. The comparative devaluations – of which there're some signs that they're emerging – could lead to some sort of major financial crisis which in turn could lead to more pumping. Then they could end up in deflation or rampant inflation. Deflation could happen if the banks are starting to pull out – then the spiral of monetary pumping by the central bank will collapse. Bank deposits will be more or less destroyed.



Source: Hedgeye

Heinz Blasnik:

I would like to comment on something Jim said. He raised the question: What is wrong with helicopter money? I think no matter which method is used, whether they spend it on infrastructure or if it's People's QE or other methods like the 'perpetual bond' – in the end it always means that they want to get something for

nothing. And that is not possible. Jim mentioned that even in infrastructure spending, which is maybe the most acceptable version of helicopter money, there's the problem that governments will waste the money. I've seen some photos of bridges in Japan that actually go nowhere.

In Europe, for instance, it is generally held that Poland is best at managing EU funds. And what they actually have done is that they have built a lot of airports that nobody is using (they are referred to as "ghost airports"). Some politically well-connected companies of course made money – for the construction work; and also the airlines that have landing slots or hubs or whatever in these airports are getting paid for having them on their itineraries. But finally everything is just a cost, these airports are not economically viable! These airports are losing money every day!

So they're endlessly wasting capital even if they build infrastructure. But the problem goes beyond that. **The problem is that the amount of real resources in an economy is finite. Governments can print money, but they cannot create real capital. So the moment governments start spending money, they buy resources and they direct factors of production in a certain direction – but this means that these factors are no longer available to anyone else, or, if they're available, they are more expensive as there's not an infinite amount of them out there.**

So the question is: What is more likely to produce wealth or prosperity? Is it going to be whatever governments do with the money? Or would it be whatever other people would have done? That is the basic problem – there ain't no free lunch. And that is what helicopter money implies: It implies that there is a kind of free lunch somewhere, but there isn't.

Jim Rickards:

I'd like to comment on that. **Heinz says it's impossible to get something from nothing. My caveat would be: It's impossible for everyone to get something for nothing all of the time, but it's not impossible for some people to get something for nothing some of the time. So certainly one can do it now, but in the end of the case that you can, it becomes a global problem.**

The way I think about these things: I certainly see the unsustainability of that. When I challenge people to tell me what's wrong with perpetual debt and central banks' balance sheets and helicopter money, it doesn't mean I agree with it – I certainly don't! But I think it's a hard thing to answer these questions. But my main point is that some people can get some benefits some of the time – that's not an economic problem, it's a political problem. **And if the political dynamic favors the handout even at the expense of the others, then we should integrate it into our inflation/deflation models, as problems probably are going to emerge.**

Heinz Blasnik:

I absolutely agree with that.

Mark Valek:

Well, what it perhaps could help is continuing the game of the musical chairs which we're playing with this monetary system. And that's perhaps the main factor why all these things are considered. **We know that we need perpetual monetary AND price to sustain this debt based monetary system.** It's becoming harder and harder to achieve price inflation. A deflationary collapse could be viewed a like a heart attack, because the flow of money doesn't work anymore. Helicopter money could be understood in the context of this analogy as a bypass surgery, with which the flow of money is reignited and the game of musical chairs prolonged.

Brent, I told you that I liked your recent presentation very much. And you assume – correct me if I'm wrong – that central banks might be late with their finger on the trigger for all kinds of measures when a deflationary event comes up, as the deflationary pressures are just too big and also the dimensions of debt and credit are just too enormous, right?

Brent Johnson:

More or less. **I completely agree that helicopter money will show up in one form or another, likely in the end of this year in Japan and early next year everywhere else (if I have to guess on timing). I think that debt levels are so high that whether it's helicopter money or whether it's more QE or whether it is even debt forgiveness in some form, they are not fixing the problem.** To a certain extent they're using defibrillators to shock the patient back awake for a few minutes, but they're not fixing the underlying problem. I don't know the academic side of it as Heinz and Jim do, **my view on helicopter money and that kind of stuff is that it may give you a short-term boost and somebody may win for some time, but it doesn't solve the underlying problem and in fact encourages the government and the central bankers to try it again later. And this would just lead to more excesses, to more misallocation of capital and sooner or later you get the big debt knockout.**

I think this goes back to Jim's comment on velocity a little bit. I don't have the empirical prove for this, but my sense is that part of the reason that it hasn't worked so far is that **the average person knows that something is wrong**, but the average person doesn't understand central banking. Maybe they see their standard of living decreasing, their jobs getting harder, or whatever – **they're saving their money for a rainy day rather than spending it senselessly. In other words: All this talk and all these extraordinary measures cause more uncertainty rather than reduce**

it, and I think that has dramatically reduced the velocity of money. If they come out now and say they print another 3 trillion, I don’t think that would change a lot. But if they print 3 trillion and they don’t do something dramatic like some debt forgiveness or sending everybody some USD 10,000 cheque and telling them they would have to spend it within the next three months, elsewise the money would be gone – maybe that would get the velocity going. **But if they do something shocking, I don’t think they get the velocity that is necessary to keep this thing going. So I think the debt burden has become so big that it will be very hard to outrun the deflationary pressures.**

Mark Valek:

Thanks for your comment, Brent! How do you view the US dollar? I guess it’s pretty important. In our opinion it may even be the most important factor regarding helicopter money. We’ve actually acted under the premise that we saw a high in the US dollar index, but it may have reversed, at least it’s pausing right now. If we see some more dollar strength coming, I think the odds of easing would increase.

US Dollar Index (weekly, including Bollinger Bands, MACD, Stochastics)

Source: Investing.com

Brent Johnson:

I think Japan will start the first helicopter money attempt and Draghi might continue before the US has to do something. **So even if the USA does something in the future, I think Japan has to do something bigger and quicker, and also Europe has to do something bigger and quicker. So even if the Fed does nothing, the US dollar has the potential to get stronger by the fact that the others are trying to weaken now.** I don't know what's going to happen during the next one or two weeks or months, but I feel there're too many deflationary pressures in the world and when those start to be attacked by Kuroda in Japan or Draghi in Europe – whenever they eventually start to break down, which doesn't seem to last more than a day or two, the US dollar will gain more strength. And I think once we have a lot more dollar strength and feel more pain at home, then the Fed could also do something. But I don't see how Yellen could justify helicopter money in the US at this time.

Ronald Stöferle:

Brent, it's very interesting that you see a much stronger US dollar accompanied by higher gold prices, so in your scenario the traditional negative correlation does not play out, which I can totally agree on.

Jim Rickards:

May I add one thing to what Brent said? Brent said that he doesn't see Janet Yellen launching helicopter money soon. I just want to make a point on that: **Central bankers do not *want* to launch helicopter money, they'll launch it by fiscal authority, meaning the parliament, the executive, the congress create some pressure. But the central banker has an important role: The central banker has to send a signal to the fiscal authority that they acquiesce, that they agree with this. The fiscal party has to be sure that once the spending is done, the central bank stands ready.** The central bank stands ready to buy as many bonds as it takes to keep the level of the interest rates. So the central bankers' role is to let the fiscal authority know that they would start to print money, but they don't initiate the concepts on the fiscal side.

Heinz Blasnik:

That's a very good point!

Brent Johnson:

Jim, this reminds me of something – maybe it was 10-15 years ago – when I got a cheque in the mail. And at that time I was just very happy to get the cheque, I didn't really think about it. It was Bush who sent out some cheques to stimulate the economy.

Jim Rickards:

Yes, Bush did a fiscal stimulus plan, I think it was in 2002, in the end of the recession of 2001, and they sent out these cheques of USD 400. This was already a kind of helicopter money. However, I remember there was no need for QE at that time as we still had positive interest rates. Greenspan kept rates artificially low, so he wasn't printing money but he was keeping rates below the market price.

Heinz Blasnik:

I'd also like to add one more thing to the discussion on helicopter money, as I think the question about inflationary and deflationary outcomes is important. I recently discussed it with some friends and one of them said: *"If the Bank of Japan really does something like issuing a perpetual bond, isn't it basically just an accounting operation? Because after all, what we're doing now is already a form of helicopter money, as they monetize one third of the public debt of the country."* What I replied to that was that the central banks have had a lot of leeway in conducting inflationary experiments because of the deflationary undertow in the system. The banking system is fragile, and the large amount of outstanding debt creates deflationary pressures.

But on the other hand, from the point of view of the public, all of this is still seen as temporary, it's dealing with the exigencies of the moment – we have a kind of emergency, so the central banks are taking special measures and so on. But somehow at the back of it there is always the implication that one day things are going to be normal again, that all these special measures are going to be taken back one day.

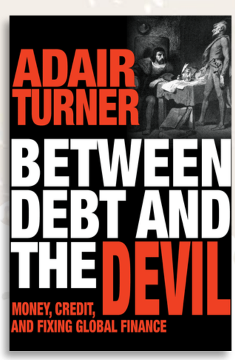
If I recall correctly, **Mises said the following: Inflationary policies can be implemented for a very long time without any consumer price inflation rising, precisely because people expect them to be temporary. And if they tend to have a high demand for money, their cash balances rise, so prices don't increase. But he also mentioned: Once the public becomes convinced that the inflationary policy is not temporary but permanent, then that is the point at which price inflation begins to take off.** Actually, in his article on helicopter money Ben Bernanke said explicitly, it must be done in such a way that the public knows it's permanent, that it is a permanent addition to the money supply.**The question then is, if they do things like introducing perpetual bonds, where is the psychological threshold at which people really start to spend money such that consumer prices take off?** One cannot know where this point is of course. Since most people don't really understand central bank policies, there is some leeway due to that as well. But there has to be a threshold somewhere and if it is crossed, people will lose confidence in the money issued by the central banks.

Source: Hedgeye

Ronald Stöferle:

Thanks Heinz!

I think we can close the topic of helicopter money. **It's noteworthy that when helicopter money entered the mainstream discussion, many market observers considered it as being illegal. However, meanwhile it has become widely confirmed that the legal hurdles are much smaller than once assumed** – you can read a quite interesting study by Deutsche Bank's George Saravelos and colleagues on this issue.



In our gold report we also summed up Adair Turner's book "Between Debt and Devil", which Jim recommended during our Advisory Board discussion in January. Perhaps it will be some sort of a playbook for central bankers. For me it was a really interesting read, although of course I don't agree with Turner's thesis. But I think it's a kind of must-read these days.

But an even more interesting perspective on helicopter money for us as Austrians has been provided by Flossbach von Storch's Thomas Mayer.

Just a technical issue: Newly printed money that is injected into the economy is a line item on the liability side of a central bank's balance sheet like also equity. This means, printing money increases the liabilities. And here's a difference between helicopter money and normal QE: Whereas for QE central banks purchase assets that outweigh the increase of liabilities that is caused by the issue of money, in the case of helicopter money they buy nothing or the so-called perpetual bonds (which finally is nothing but thin air). This means that either they artificially blow up their balance sheets with perpetual bonds or their equity capital decreases instead and – when they do it repeatedly – will finally become negative. So Mayer points out that, whilst this would be the bankruptcy for any normal kind of company, central banks could do this, as their main asset is neither gold, nor government bonds, nor whatever, but *trust capital*.

As long as people trust into the money that central banks issue, the currency will be used and work fine; if trust reduces, people will try to spend the money, velocity increases and we have inflation (so basically what they want to achieve to some extent at the moment). However, if helicopter money is used to pay off debt, debt could be reduced and this whole thing would change the monetary system from a credit money system to a reputation money system, how Mayer calls it. And reputation money is for instance also gold or Bitcoin. **So according to Mayer helicopter money could also blaze a trail for a reputation money system in which different types of money compete with each other – as also Hayek proposed in "The Denationalization of Money". So the argument is that helicopter money could be the trigger for an institutional change of the monetary system and at the end there would be different forms of money and people just choose which type they prefer.**

Now let's touch a different topic. There has been a major shock in the second quarter which has made the situation even more chaotic: the Brexit. Whereas the initial impact of the referendum could have been digested quite well, uncertainty in the markets has increased for the longer term, especially as the crisis of the EU is getting a new dimension and many complex processes have been set in motion that threaten this political project. Zac, as you are the Brit amongst us, maybe you can let us know how you evaluate the situation?

Zac Bharucha:

Well, what I'm aware that financial markets are a symptom of the broader socio-economical and cultural landscape. I see deterioration. Concerning Brexit I think, **with the policy shift that took place after the 2008 financial crisis – maybe it's an unintended effect, maybe it's an intended effect –, there has been an increase in**

inequality, as there's been an exclusion of many citizens from the economic machine. I think there's also a widely shared perception that something is going wrong with the economic machine: The pace of post-crash recovery has been really weak, in the US it's one of the weakest recoveries, and it has come at the cost of massive suppressed inflation. There's something not quite right in this economic development, and so far in the current 'tightening' cycle, we've had one rate rise in the US, nothing much elsewhere, plus the Fed backpedaled with quantitative easing. **Elsewhere they're still pumping, which again is fuel for asset prices and doesn't yet emerge in consumer prices – so the wealthy and highly paid employed are getting more wealthy, and those who are outside the financial bubble are more and more at odds with it. It's a class war.** You can look at the migrant crisis through this prism, it's exposing fractious behavior within the European countries as more and more are moving back to nationalism – I think the EU project is very difficult to sustain. Brexit came as a total shock to the technocrats – the political leaders, the economists, the class of experts –, who all thought that the plebs would do what they were told. **But I think that what the Brexit voters did was react most savagely to received wisdom. I suspect that plebiscites in other countries would also spite the technocracy and reveal deep divisions. And these divisions are as follows: young people against old, between those connected inside the economic system versus those disconnected outside the system and the very division between bourgeois or middle-class people with education working in cozy professions against the class who actually have to compete with low-cost labor from the East. In Britain the working class are totally exposed to this with scant union or guild protection. Why on earth would they do as the establishment told them?**

So what's the relevance of this for those of us who are looking at markets? There is tension here. The 'old world' globalization plus liberal market democracy, emphatic in its realization of the individual within a social Darwinist construction, blunders along empty headed eight years after the last crash.

I think the EU might have to give up its ideal of free movement of people. If they don't, other countries with secessionist tendencies, might follow the Brisitsh and will pull the system down. The core political parties are in retreat because they have failed huge sections of the public who are stung by globalization. The EU has promoted globalization as it has benefitted the bourgeois, the construction is applauded by America because it is convenient short-hand to deal with a pro-US continent as one bloc.

I think the growth prospects for Europe are bad. It's a nice place to live due to the remnant of social democracy, but I'm very troubled about the return of nationalist and ethnic sentiment.

Naturally, the BoE will do more money pumping. Anytime there's a hint of any kind of problem, central banks again – the unelected the bastions of monetary control – will step in and basically do more QE. I think this tool of magic money is not going to be put away.

Ronald Stöferle:

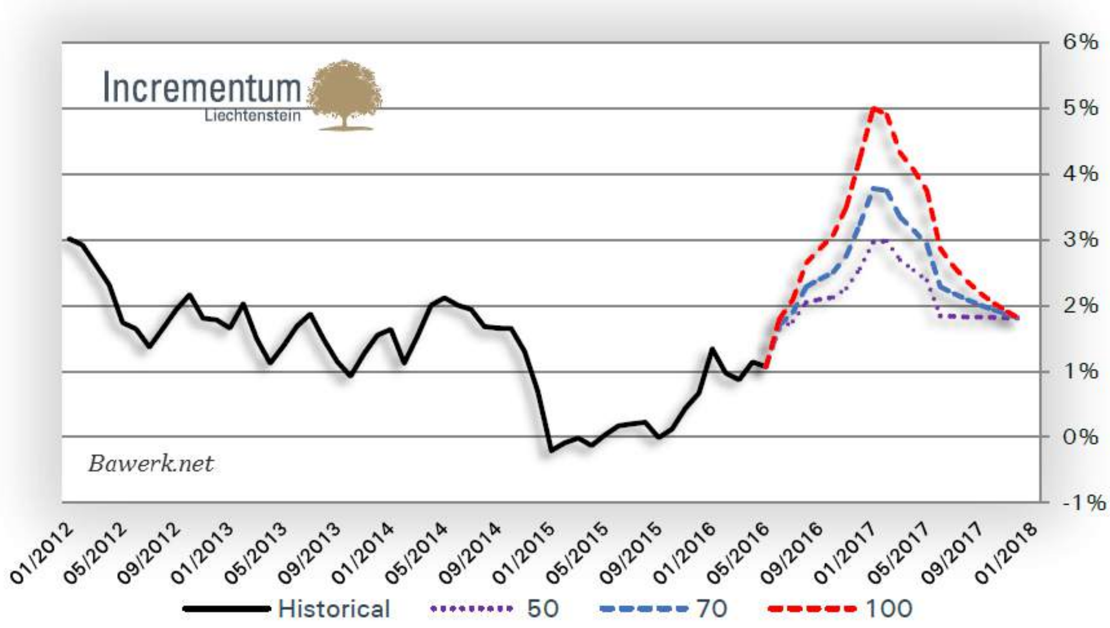
Thanks Zac for your thoughts on this! I totally agree that these centrifugal forces within the EU and the Eurozone will jolt the system and the continent. And I also think that they have the potential to either lead to a catastrophe or to induce fundamental reform – while the Junckers & Co. don't appear to have understood the signs of the times.

Gentlemen, for the last round we would like to discuss your best trading ideas and most interesting positions for the second half of the year. Heinz, would you like to start?

Heinz Blasnik:

Well, in the short term I've shorted US Treasuries for a correction. I don't know how far it's going to go, but I think it has a bit further to go than it has gone so far. The main reason for this is that consumer inflation indexes like the CPI and the harmonized CP index in Europe are going to be higher in the second half of the year because of the moves in the oil price – that's just a matter of base effects. You can already see it: CPI in the US already increased to 2.3% yoy, so it's actually above the Fed's target already. And in Europe we could see it going to something like 1%, which is a lot higher than it is now (I think now it's currently 0.3% yoy). And experience shows that the bond markets actually do react to that.

Annual Change in Headline CPI for Various Oil Price Scenarios



Sources: Bureau of Labor Statistics (BLS), Federal Resreve St. Louis, Bawerk.net, Incrementum AG

Then in the medium term, I think (or I hope) there's going to be a bigger correction in gold. **At some point in the second half there should be a correction in gold and we should have the opportunity to buy gold and gold stocks, so I wouldn't chase them now but I think there's going to be a good opportunity in the second half.**

And another thing, I'm looking for a market weakness at some point in spite of the fact that the S&P 500 and the Dow Jones Industrial Average have broken out. None of these breakouts have been confirmed by any other markets, so they look very suspicious to me and I think the complacency is very pronounced right now – in the US markets specifically.

And I'm also still thinking that **in terms of equity markets, emerging markets offer the best opportunities, because there you still have some markets or stocks that are actually cheap. They also look better technically. And there's also some upside in their currencies as well in the short term.**

Mark Valek:

Thanks Heinz! Zac, what are your thoughts?

Zac Bharucha:

I observed that in countries that have weak currencies, the stock markets tend to do better. We saw this for a long time in Japan. **And then you see, as soon as the currency starts to strengthen, the equity market loses vigour.** So you have to follow a kind of currency hedge strategy if you want to try to play along with the equity market moves. The bond prices are obviously at ludicrous extremes now.

Hold gold! If you trade one paper currency vis-à-vis the other, there are these fits and starts, where suddenly the dollar is a bit stronger, then it's a bit weaker, the next minute it's the pound or the yen – wherever the action is –, this is chasing smaller moves in exchange rates. And really, gold now has reestablished an uptrend. I got the entry point really nicely at the USD 1,050 to 1,100 level. And I think this is a core portion of the portfolio – **for me it is the core long-term investment. And with that I would include to a lesser degree also platinum and also silver as alternative assets.**

I think the housing prices continue to remain in a bubble, but the policymakers will do everything to keep the bubble up. But rest assured, those long are playing with fire. For me the markets are pretty dull because in this situation the fabric is so manipulated and artificial, it remains a sort of Alice in Wonderland, guessing what in particular central banks might do next. It is difficult to say something meaningful other than "It's all a mess". And people in power will continue to make a mess rather than reform, they will continue to try to maintain this status quo. How does that impact us as asset allocators, market traders or investors? I think it's reasonable holding that core gold position and looking for tactical opportunities. **I think there's probably going to be a kind of crunch again in the markets, I think the sentiment is very fragile. In the stocks, the last thing we see in the US S&P is a new high.** But if you look at the FTSE, it's still below its all-time high, the Nasdaq too, and there are some more divergences – the DAX is obviously decoupled and is well off the highs.

Germany stands to lose the most from Europe with free movement and free trade coming to question. I think the German economy stands to be one of the bigger losers. So in tradable terms, I would have some short positions in the DAX vis-à-vis other markets. In Japan, I would buy the Nikkei on a hedged basis on the 14,000 to 14,500 level – so if we have the usual autumn bust, get long. And sectorwise, I think the gold sector and basic metals perform well from here.

Ronald Stöferle:

Thank you very much, Zac! Someone else? Brent?

Brent Johnson:

I kind of agree with what has been said before. The miners have had one heck of a run and in some cases it might be justified, in some cases it is not. I think we all agree upon gold is getting higher, so if you don't own any you should definitely get some. **But in the short term I would not chase in here. I think we will get the chance to buy them at a lower price sometime in the next 3-4 months. And even if you don't get the chance to buy them at a lower rate in the next few months, you might be able to buy them with a lot more certainty.** Maybe you'll also pay up for more certainty, but I'd rather pay up for more certainty than chasing here with the chance of buying them lower as well.

One company that I do like because it has tremendous potential is GoldMoney. You know it started of as BitGold and then they acquired James Turk's GoldMoney. **I like it for a couple of reasons. First, they have a traditional gold storage business, which I think is going to increase in value in the years ahead. Second, they also have a technological platform that allows for gold being used in a payment system.** Obviously Bitcoin is big in the payment system, there's Apple Pay and all that different stuff which is USD-based (apart from Bitcoin). I think they come up with a very interesting way for payments, cross-border payments, round-the-world payments in a very quick and efficient manner using gold. I think the optionality on that is absolutely huge. **And the third point why I like them is, they probably got the best all-star team in the world.** I have never seen all of them together in the same room – but if they can somehow work together and sum up all this brainpower, then what they can accomplish would be absolutely massive. So I think it's going to either be a big business or a very, very big business. **So I would recommend buying shares in GoldMoney.**

Ronald Stöferle:

Once a very successful trader told me: If something should go down and correct but just doesn't go down, double your bets. And I think gold is so resilient and so strong, everybody knows that it's massively overbought and that the sentiment doesn't come down, that's a great sign. And there are so many market participants on the sidelines because no one of these private bankers and asset managers participated in that first move in the first quarter. We wrote in the gold report that based on the Dow Theory, first there's the accumulation phase where the smart money is buying, and then comes the public participation phase when the media is picking up the topic again and all the mainstream banks are upgrading their price targets and so on. And we're now in the beginning of this public participation phase. So if we end the year at 1,400 to 1,450 that would have been a great year. **I think**

for the mining stocks, as they really did their homework in the last few years during the correction, their leverage on rising gold prices is even higher than back in the days.

Brent, you made a terrific recommendation last time with your call on Reservoir Minerals. It got taken over a couple of days later or the bid was increased, I think.

Brent Johnson:

Yes, this was a pretty good timing.

Ronald Stöferle:

Concerning GoldMoney, we totally agree: It's a great business, it's a great team – we've known James Turk for many years now, I really like Alasdair Macleod, John Butler of course and also Josh Crumb and Roy Sebag seem to be really smart and ambitious. So I totally agree, it's a great business and probably a great investment at this point.

Brent Johnson:

I have something to add. I don't think this kind of stuff gets talked about enough: Peter Schiff came about half a year ago out and kind of boasted GoldMoney for being inferior and whatever it was – it was just a kind of unnecessary criticism I thought. But rather than taking revenge or challenging Peter Schiff in that debate, that started a dialog and now they had a sort of a merger. Well, I always said the outside versus the inside is so small and it makes no sense for us to argue with each other – we should rather help each other and make each other successful to bring gold to the rest of the world. And I was really impressed that rather than creating a big fight they tried to learn from what Peter was saying – and to Peter's credit, I think he realized that he was wrong. **That was probably more impressive for me than any of the financial stuff, to be honest.**

Mark Valek:

Well, Peter Schiff is pretty much a marketing machine in the US, he has a big mouth but he also has good points. I like him very, very much, but he has his own style.

Heinz Blasnik:

And it is impressive what has happened because he's actually quite combative. So to get him to the point that he really admits that he wasn't really correct in his first assessment is really quite a feat.

Ronald Stöferle:

Frank, what are your best ideas for asset allocation for the second half of the year?

Frank Shostak:

My econometric models still remain quite bullish on the stock indexes. But if I look from the asset allocation perspective or from a more conservative perspective, then one probably would need to exercise caution in terms of stock markets, because they're really going crazy.

And I think gold on a trade basis could be okay, but not the other commodities. I don't see much joy in oil.

Ronald Stöferle:

And from a currency perspective, which currency would you favor most at the moment?

Frank Shostak:

For the US dollar against the euro, I don't see very much. By December I see a rate of 1.09, and by December next year I forecasted 1.07 – so that's not very much of a trend.

Considering the yen against the dollar, the yen could still strengthen until year end and next year we can see quite a strengthening in the dollar against the yen or a weakening in the yen against the dollar. This December it could be at 1.01 yen to the dollar, then by September next year the forecast is almost 1.40.

Now when we have a look on pound sterling, this whole story with Brexit and all these things didn't really matter much I guess. And so it probably will stabilize around 1.30 US dollar to the pound and so it will hover there.

I see that the Swiss franc could weaken against the dollar by March next year, but thereafter it tends to strengthen: By December next year it could be at 0.95. That's not hell of a lot.

And for the dollar I don't really see much. It could stay in this range of 0.74 and something. By June next year it could rise to 0.77, that's what the model shows, and thereafter it would weaken to 0.74.

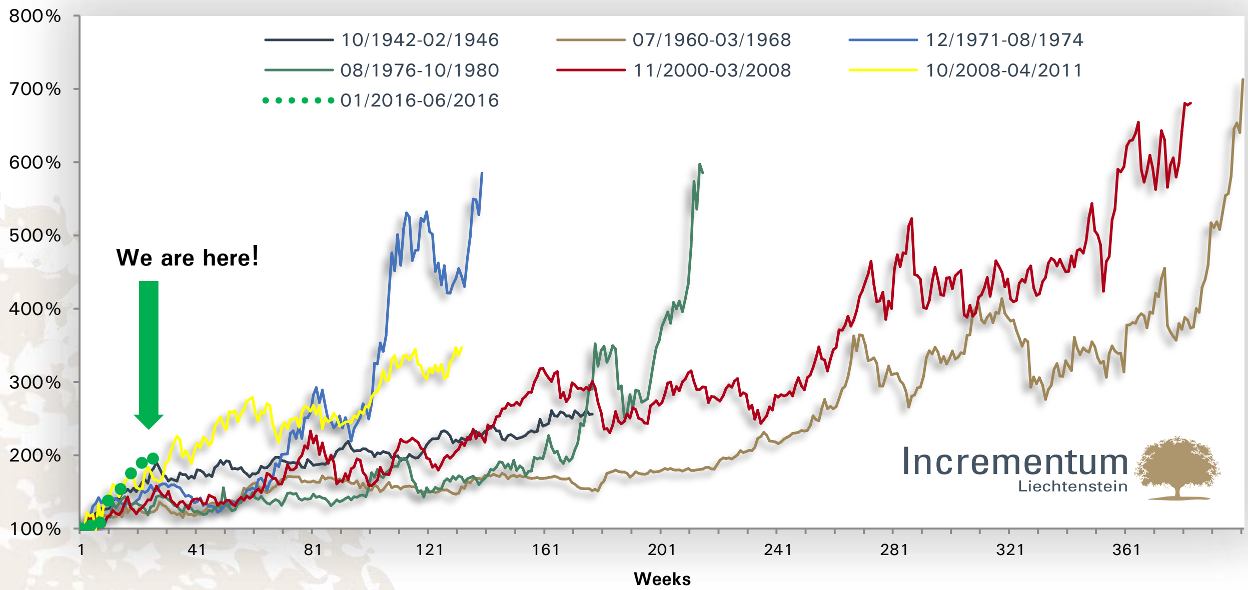
Mark Valek:

Jim, do you have some final words?

Jim Rickards:

Yeah, **I also like physical gold and GoldMoney.** Brent and Heinz are quite correct that it's had quite a run and whenever you see that, it makes you reluctant to jump in. But I've seen some historical tables with a lot of bull markets in gold mining stocks. Where gold mining stocks stand today barely registers to the historical pattern of gold mining stock bull markets. **I would make the point that we are not near the top, it's quite close to the beginning – so I'm very bullish on that sector.** So that's the basics: I like gold and gold mining stocks.

Bull markets compared: BGMI bull markets since 1942



Sources: Sharelynx, Nowandfutures, Barrons, Incrementum AG

I agree that there are some signs of inflation out there – that is no news in the whole inflation / deflation sort of thermometer or barometer that I use and you guys use; it ticks back and forth, it's just the nature of it. You can't be too categorical or too dogmatic one way or the other because both forces are very much present at the same time. **Right this minute, my own view is that inflation is getting a little bit an uptick which is going to put pressure on bond prices, except the Fed Reserve** – and I think it all comes down to the Fed, as 80% of global payments and 60% of global reserves are dollars. So whether you like it or not, the world economy is a dollar economy and the Fed controls the dollar – that's just the starting point of the analysis, however unhappy that state of affairs may be. And the Fed has a bias towards raising rates. That doesn't mean they're going to raise rates anytime soon. But they will raise rates when they see the opportunity. So a little bit of inflation combined with continued good job growth and a positive economic performance could be a trigger for the Fed to raise interest rates, not before December, but maybe in December even or early 2017.

That would be exactly the wrong policy at exactly the wrong time, which is: **US economic growth is fragile, the Fed should be looking for ways to ease by going back to zero or cheapening the dollar; but they are not, they are looking for ways to tighten. And that's just enough to drive the nail in the economic coffin, so to speak. It's turning the US into recession, which should send the Treasury Note a lot down, which would be one of the biggest bond market meltdowns in history.**

Mark Valek:

Okay, thanks Jim!

I think we can close the discussion at this point. Thank you very much, gentlemen, for another very interesting discussion! We will have the next call probably in the heat of the presidential election in the US, so that could be fun as well.

Ronald Stöferle:

Gentlemen, also from my side, thank you very much! I think it's going to be a very interesting fall and winter, so I'm really looking forward to our next discussion!

Appendix A: Members of our Advisory Board:

Special guest: Brent Johnson

Brent brings over 15 years of experience in the financial markets to his position as CEO of Santiago Capital. He has been creating and managing comprehensive wealth management strategies for the personal portfolios of high-net-worth individuals and families since the late 1990s. The lack of an appropriate precious metals solution for his clients is what led him to create and launch the Santiago Gold Fund LP in January 2012. As a recognized expert in the gold community, Brent's views have been quoted in numerous print, online and television outlets. In addition to managing Santiago Capital, Brent is a Managing Director at Baker Avenue Asset Management. Before joining Baker Avenue, Brent spent 9 years with Credit Suisse as vice president in their private client group. Brent played on the junior varsity basketball team at the University of Kansas before transferring to Rockhurst College in Kansas City, where he graduated with a dual degree in economics and global studies. He received his M.B.A. from Thunderbird School of Global Management. Brent lives in San Francisco with his wife Mary and son Moses.

James G. Rickards

Jim is the author of the international bestsellers *Currency Wars* and *The Death of Money: The coming collapse of the international monetary system*. He is portfolio manager at the West Shore Fund. During his career, Jim has held senior positions at Citibank, Long Term Capital Management and Caxton Associates.

Heinz Blasnik

Heinz is an independent trader and market analyst for the consulting firm Hedgefund Consultants Ltd, as well as a regular publisher for the Independent Research House Asianomics in Hong Kong. Heinz primarily is responsible for his blog www.acting-man.com, on which he analyses developments in the financial markets from an Austrian point of view.

Zac Bharucha

Zac began his career in finance at the investment bank Kleinwort Benson and later became an equity portfolio manager at Philipps and Drew Fund Management. He then moved to AMP Asset Management where he was responsible for managing more than GBP 1bn of institutional assets. Afterwards, he moved to M&G in London. Since 1998, he has developed absolute return strategies and specialized in equities and commodities. After 25 years in asset management, he retired from professional life in 2011 and wrote his first book about market timing.

Dr. Frank Shostak

Frank is chief economist at AAS Economics. He has over 35 years of experience as a market economist and central bank analyst. He holds a PhD, MA and BA honours from South African universities. He was professor of economics at the Witwatersrand University in Johannesburg. He is one of the world leaders in applied Austrian School of Economics and an adjunct scholar at the Mises Institute in the US.

Rahim Taghizadegan

Rahim is the founder and director of the institute for value based economics, an independent research institute in economical and philosophical issues in Vienna. He is bestselling author and a popular speaker internationally. Rahim studied Physics, Economics and Sociology in Vienna and Lausanne. He has worked in the fields of economics, space research and journalism. He has also taught at the University of Liechtenstein, the Vienna University of Economics and Business Administration and the Universität Halle an der Saale.

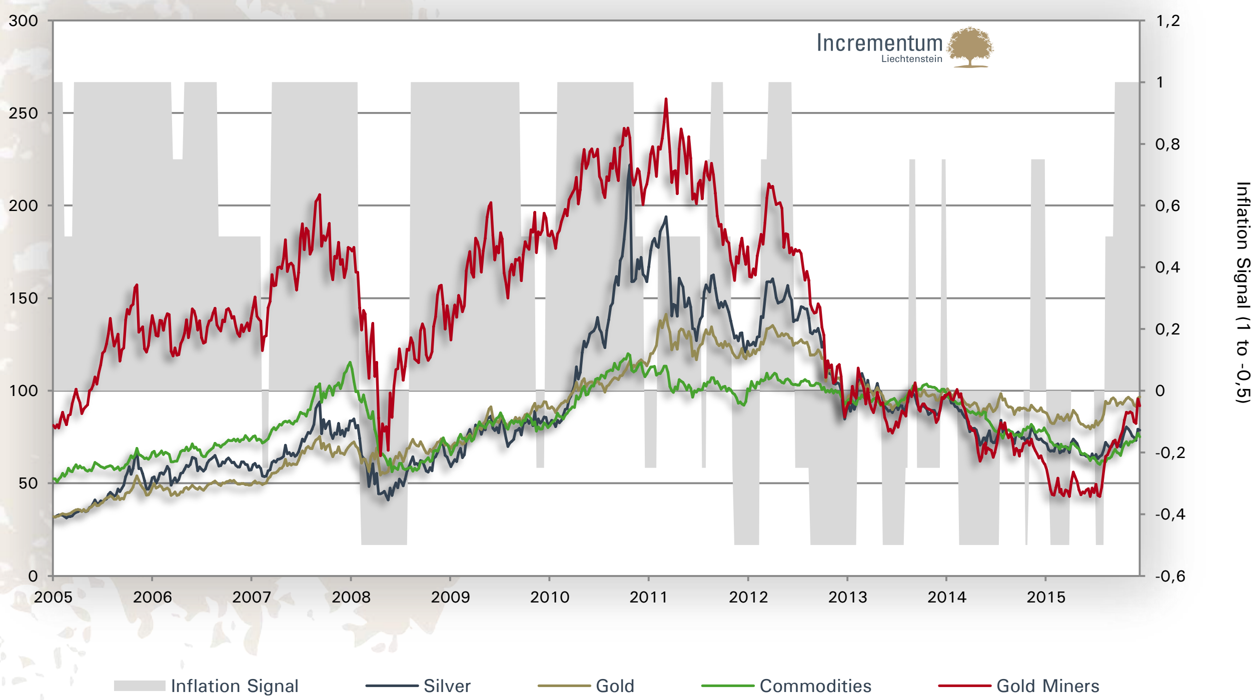
Incrementum Inflation Signal

At Incrementum, we are convinced that inflation is a monetary phenomenon. Because of the dynamics of "monetary tectonics", inflationary and deflationary phases can alternate. **To measure how much monetary inflation actually reaches the real economy, we utilize a number of market-based indicators** - a combination of various quantitative factors including the Gold-Silver Ratio - which result in a proprietary signal. This method of measurement can be compared to a "monetary seismograph", which we refer to as the **"Incrementum Inflation Signal"**.

In the fund we manage, our Incrementum Inflation Signal gauges the inflation trend and we position the fund accordingly. Historically, we observed periods of between 6 and 24 months during which disinflationary forces were dominant. These phases were particularly painful for the holders of inflation sensitive assets.

The signal is exclusively based on market-derived data and has a shorter reaction time than the usual inflation statistics. Depending on the signal's message we shift allocations into or out of inflation-sensitive assets – primarily mining stocks, commodities and energy stocks. **Currently, the Incrementum Inflation Signal indicates that a full-fledged inflation trend is underway.**

Incrementum Inflation Signal



Source: Yahoo Finance, Incrementum AG

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