

ments that would preclude frequent recurrences of such gold rushes. One wonders how many similar scrambles for gold we are able or willing to endure.

Official switches from dollars to gold have sometimes taken place without any provocation from private speculation. The most conspicuous moves were, of course, those of the two largest European owners of gold, Germany and France. In the years 1964 and 1965, Germany reduced her foreign-exchange holdings by almost one half and increased her gold stock. France did the same thing in 1965 and 1966. Not all but most of their accumulations of gold cut into the gold reserves of the United States. There has been none of such official switching in recent months, if we disregard the action by Algeria. On the contrary, the major monetary authorities have realized that they had better stabilize the boat rather than join in rocking it. Germany, especially, has cooperated with the United States as the Bundesbank accumulated large amounts of dollars. Similar accommodation has been received from Italy.

This kind of bilateral accommodation, however, is no solution to the problem of confidence. A viable situation can exist only if massive raids on official gold holdings are excluded by institutional changes.

THE PRIVATE DEMAND FOR GOLD

There exists widespread confusion concerning the increase in private demand for gold. Observers often confuse speculative purchases with long-run demand. They also fail to distinguish increases in the demand for gold that are associated with decreases in the demand for dollars from gold purchases that do not involve reductions in private dollar holdings.

When the Council of Economic Advisers observe that our "deficit may have been increased further indirectly by the flurry of private gold purchases," they probably assume that these gold purchases were financed, directly or indirectly, by capital outflows from the United States. This is only a very small part of the picture. Perhaps they mean that many foreigners would be more interested in American securities if they were not so crazy about buying gold. In this sense it is true that our balance of payments is worsened by the gold rush. On the other hand, when private foreigners use their dollar balances to pay for the gold, both our dollar stocks and our liquid liabilities are reduced, and the balance is unchanged.

I believe the Council also overestimate the industrial use of gold when they figure that it was about \$750 million last year. Since even industrial processors of gold may be speculators in their inventory policies, it is possible that industrial purchases in 1967 were unusually high. But that the current use of gold for industrial purposes, including jewelry, is much less, can be gathered from the known figures for the United States. In 1965 industrial users of gold in the United States purchased \$185 million worth of gold. Statistics are available for only eleven other countries; the rest has to be guessed, and the total was estimated at \$300 million. I doubt that the total for the world reached \$500 million in 1967—which still would have been less than one-third of the gold production in the western world.

The remainder was probably divided between traditional gold hoarders and speculative gold buyers. The difference between them is that the traditional buyer acquires gold regardless of its price and of expectations concerning increases in the price, whereas the speculator buys because he expects the price to increase. He would probably sell again after the expected increase has taken place or after he has resigned himself to the fact that his expectation had been wrong.

The stupidity of persistent gold speculators is incredible. If a speculator bought his gold in 1954, his investment by the end of 1965 would have been worth less than one-third of what he would have owned had he purchased an average portfolio of American industrial stocks. A speculator who bought his gold only in 1960, would have found at the end of 1965 that his investment was worth less than one-half of what he could have had if he had purchased a Dow Jones mixture of industrial stocks. Even if his hope of a doubling of the price of gold had come true at the end of 1965, he still would not have made as much as an investor in American stocks.

I have not carried my calculations to December 1967, but they would unquestionably put the gold speculator still further behind the average investor in the New York Stock Exchange; the gold buyer of 1954 probably has now only one-fifth of the shareholder's present worth.