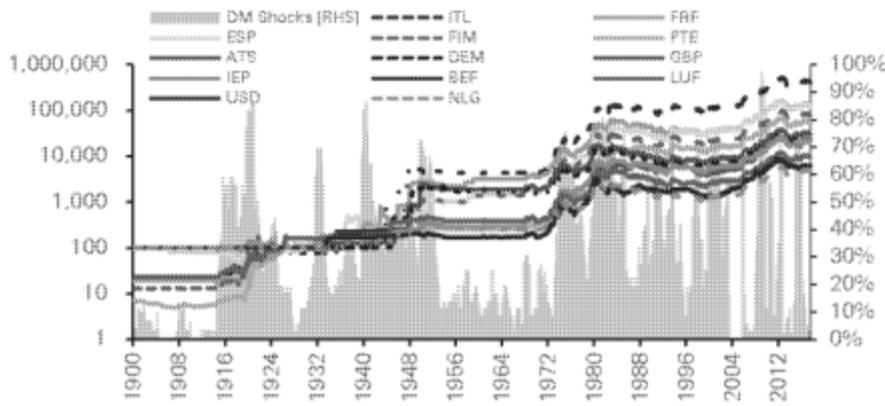




- The various breaks with gold based currencies over the last century or so has correlated well with our financial shocks/crises indicator. It shows that you are more likely to see crises/shocks when we break from hard currency systems. Some of the devaluation to Gold has been mindboggling over the last 100 years.

Figure 4: Gold Prices in various currencies (Dec 1925 = 100, Y-axis in logarithmic scale) and DM Financial Shocks (RHS)



Source: Deutsche Bank, Global Financial Data, Bloomberg Finance LP

- Perversely, the current post Bretton Woods system also allows for huge operations/stimulus to overcome any crisis/shock. We also shouldn't underestimate the positive impact that this can have on nominal asset prices. Cash is arguably a far more dangerous asset in a fiat currency but unstable regime than it is in a more stable less crisis prone one. However, by continually using stimulus to deal with crises and not letting creative destruction take over, you make a subsequent crisis more likely by passing the problem along to some other part of the global financial system, and usually in bigger size. In a fiat currency world, intervention and money creation is the path of least resistance. In a Gold standard world, mining new gold was the only stable way of increasing the money supply.
- We think this leaves the current global economy particularly prone to a cycle of booms, busts, heavy intervention, recovery and the cycle starting again. There is no natural point where a purge of the excesses is forced by a restriction on credit creation.
- So we're quite confident that there will likely be another financial crisis/shock pretty soon with their frequency continuing to be high until we create a more stable global financial framework.

So where will the next crisis come from?

- An obvious issue is how we resolve the combination of the unwinding of unparalleled central bank balance sheet sizes at a time of record peacetime government debt and multi-century record low yields (Figure 5).