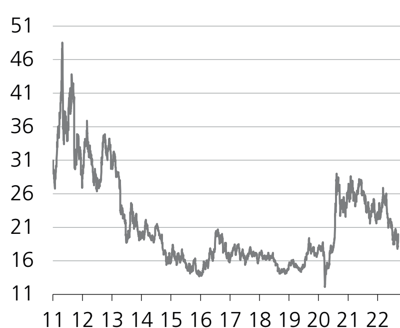
Degussa Market Report

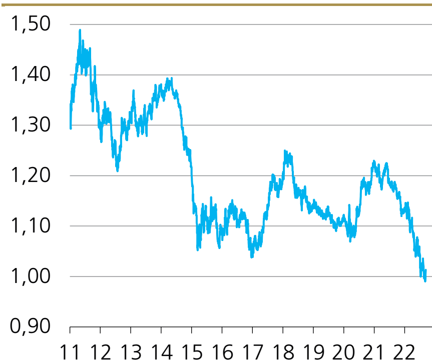
15 September 2022 Economics · Finance · Precious Metals

USD per ounce of gold

USD per ounce of silver



EURUSD



Source: Refinitiv; graphs by Degussa.

Precious metals prices				
	Actual (spot)	Change against (in percent): 2 W	3 M	12 M
I. In US-dollar				
Gold	1.689,1	-2,8	-8,1	-3,8
Silver	19,5	3,1	-9,6	-12,3
Platinum	908,2	5,2	-5,9	-5,7
Palladium	2.147,2	1,7	7,4	12,4
II. In euro				
Gold	1.692,4	-2,9	-1,1	11,6
Silver	19,5	2,9	-2,7	2,0
Platinum	909,9	5,1	0,9	9,3
Palladium	2.151,0	1,7	15,4	30,5
III. Gold price in other currencies				
JPY	242.551,0	1,6	2,6	24,1
CNY	11.776,0	-1,3	-3,9	4,0
GBP	1.464,4	-0,9	0,5	12,4
INR	134.380,1	1,9	-5,7	3,2
RUB	100.760,2	-2,2	-9,0	-21,0

Source: Refinitiv; calculations by Degussa.

OUR TOP ISSUES

*This is a short summary of our fortnightly **Degussa Marktreport**.*

INFLATION, HIGH INFLATION, HYPERINFLATION

The word "inflation is heard and read everywhere these days. However, since different people sometimes have very different understandings of inflation, here is a definition: "Inflation is the sustained rise in the prices of goods across the board."

This definition conveys that inflation means that the increase in prices of goods is not just a one-off but permanently; and that not just some goods prices go up, but all.

How does inflation arise? The economists have two explanations ready. The first explanation is the "non-monetary" explanation of inflation. According to this theory, sharply rising energy prices lead to inflation. This is referred to as cost-push inflation. Or inflation is caused by excess demand: the demand for goods exceeds the supply, causing prices to rise.

The second explanation for inflation is monetary. "Inflation is always and everywhere a monetary phenomenon," as US economist Milton Friedman put it. And that's right. Because in an economy without money, there is simply no inflation. So you can see: Inflation has something to do with money.

It can be demonstrated theoretically that an increase in the money supply leads to an increase in goods prices – the prices of goods will be higher compared to a situation where the money supply has not been expanded.

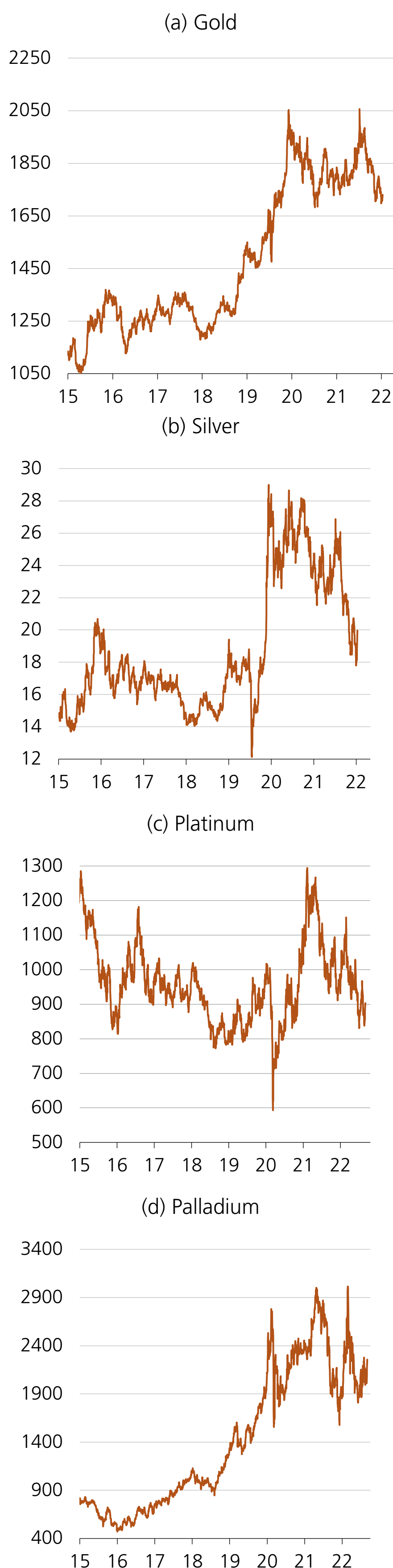
There is quite some empirical evidence that increasing the amount of money over time is associated with rising goods prices – be it in the form of consumer goods prices and/or asset prices such as stocks and real estate.

With a view to current developments in the world, however, both explanations can be meaningfully connected.

The energy price shock triggered by green policies, which has many other commodity prices skyrocketing, combined with lockdown related shortages in many commodity and goods markets, are hitting a huge monetary overhang that central banks have built up over the past few years.

And it is precisely this monetary overhang that makes it possible in the first place that the goods price shock can translate into inflation – i.e. further increases in goods prices across the board.

Precious metal prices (USD/oz), last seven years



Source: Refinitiv; graphs Degussa.

From this perspective, it is the excessive monetary overhang that is responsible for goods price inflation. Without it, this kind of inflation would not have been possible; without it, there would be no continued increase in all goods prices.

It should therefore be emphasized at this point that when talking about inflation, it makes sense to distinguish between goods price inflation and money supply inflation. Goods price inflation is the symptom, and money supply inflation is its cause.

We know that inflation means a loss of purchasing power of money: When there is inflation, you get fewer and fewer goods in exchange for your money. In today's unbacked paper money system – the fiat money system – inflation is chronic, a daily plague, so to speak.

The reason: state-sponsored central banks, which have the monopoly of money production, have set themselves the goal of delivering inflation of 2% per year. This may seem acceptable at first glance, but not at second glance.

Because in doing so, central banks do not preserve the purchasing power of money over time; they deliberately reduce it! They are not currency guardians but currency destroyers.

An inflation of 2% may seem "small". But over time, it leads to a considerable reduction in the purchasing power of money.

For example, with an inflation rate of 2% per year, the loss of purchasing power of money is 9% after 5 years and 18% after 10 years.

Inflation of 5% will already have destroyed the purchasing power of money by 22% after 5 years and by 39% after 10 years.

And with 10% inflation, 38% of purchasing power is obliterated after 5 years, and 61 % after 10 years.

What is high inflation? Well, there is no single definition for that. But it makes sense to speak of high inflation when the goods prices increase by 5, 10 or 15% a year.

We speak of hyperinflation when the rate of increase in the price of goods is very, very high and continues to increase over time; we could also say: when it starts galloping.

Most modern economics textbooks state that hyperinflation occurs when prices increase by 50% or more per month. This definition goes back to the influential work of the US economist Philip Cagan.

However, be aware that a price increase of 50% per month implies an annual inflation rate of almost 12,900%. That's frighteningly high. It would mean, for example, that the price of a cup of coffee would increase from 3 US dollar to 390 US dollar within a year.

In view of the devastating effect of hyperinflation on the purchasing power of money in a very short time, it makes economic sense to set the threshold much lower – and to speak of hyperinflation already when there is a permanent price increase of, say, 3 % per month.

How does hyperinflation occur? The phenomenon of hyperinflation was brought upon the world with unbacked paper money, with fiat money. Hyperinflation was and is inextricably linked to fiat money.

The reason is that the state central bank can, simply put, increase the amount of fiat money at any time and by any amount.

And that usually happens, as currency history painfully shows, when the state is at war or when it is so over-indebted that it sees no other way of financing its spending than to literally have its central bank print new money.

Hyperinflation is usually triggered for political reasons. The economist Ludwig von Mises put it succinctly when he wrote in 1923:

"We have seen that if a government is not in a position to negotiate loans and does not dare levy additional taxation for fear that the financial and general economic effects will be revealed too clearly too soon, so that it will lose support for its program, it always considers it necessary to undertake inflationary measures. Thus inflation becomes one of the most important psychological aids to an economic policy which tries to camouflage its effects. In this sense, it may be described as a tool of antidemocratic policy. By deceiving public opinion, it permits a system of government to continue which would have no hope of receiving the approval of the people if conditions were frankly explained to them."

I will now briefly outline how inflation escalates into high inflation and hyperinflation.

Let us assume that the state is heavily indebted and gets into financial difficulties – because, for example, the economy is in recession. The state's revenue is drying up, and there is a big gap in its budget. To close it, the state issues new bonds, which the central bank buys and pays for with newly created money.

The state spends the money (on employment programs, social transfers, etc.), and the amount of money in the hands of consumers and producers increases. The recipients of the new money then exchange it for goods, causing the prices of the goods to rise as a result.

However, people were literally taken by surprise by the sudden increase in money supply and the resulting increase in goods price inflation: actual inflation is higher than originally expected, i.e. higher than the inflation promised to them by the central bank.

The "surprise inflation" has caused the price of goods to rise more than wages and pensions, making the general population poorer. Their real, i.e. inflation-adjusted wages and incomes are falling.

People see the scam and realize they have been tricked by surprise inflation. As a result, they adjust their wage, rental and loan contracts by renegotiating them based on higher inflation expectations.

If the state does not cut its spending in this situation, but increases it even further, for example, because the payments for social transfers (housing benefits, food subsidies, etc.) continue to increase due to higher goods price inflation, an ever greater expansion of the money supply courtesy of the central bank will be the consequence.

Suppose the central bank increases the money supply (by, say, buying even more government bonds). In that case, people will be hit by surprise inflation again, and the purchasing power of their money will be eroded even more.

The ongoing central bank fraud will sooner or later eat away confidence in the currency. As a result, people reduce their cash holdings. They increasingly demand other goods in exchange for their money. This, in turn, amplifies the general rise in goods prices, and the rising goods prices and the falling demand for money reinforce each other.

It won't be long before the expectations arise that the central bank will expand the money supply at ever faster rates – from, say, 10 % this year to 15 % next year, then to 25 % the following year, then to 40 %, and so on – and that it never ends. Eventually, the "flight out of money" sets in.

A "crack-up boom" unfolds, with people eager to exchange their money for all valuables that are still available (stocks, real estate, watches, precious metals). In extreme cases, the purchasing power of fiat money collapses, it ceases to be used as money, and the money holders and savers suffer a total loss.

Can the hyperinflation process be stopped? The answer is: theoretically, yes. The central bank just has to stop expanding the money supply. But it is precisely this measure that usually encounters fierce political resistance, especially when high inflation has already set in.

Above all, people dread national bankruptcy, the economic and social crisis and the chaos that would ensue. The state-appointed central bank councils consider it their duty not to let the state go bankrupt in an emergency, even if that destroys the value of money.

In highly indebted, extensive welfare states, the danger of hyperinflation is particularly great – because here, very many people depend on the financial handouts of the state and prefer – at least initially – that the state remains liquid, even if it means rising inflation.

At some point, however, the economic costs of hyperinflation will become unbearable. In that sense, hyperinflation cannot go on forever. Either it ends with stopping any further increase in the money supply, rescuing the currency from complete collapse, allowing a crisis to clean the slate – as happened in Austria in early 1923.

Or it ends with the purchasing power of money being completely destroyed, and the thus destroyed currency being replaced by a new one as part of a currency reform (as in the Weimar Republic, the Deutsche Mark was replaced by the Rentenmark in November 1923).

Or by literally removing a lot of zeros from the banknotes – as happened in Turkey in 2005, for example, when six zeros were eliminated from the banknotes, and the bank accounts were adjusted accordingly (e.g. 1 million Turkish lira became 1 new Turkish lira).

Now you may be wondering: is hyperinflation imminent? It cannot be overlooked that inflation has already turned into high inflation. In July 2022, US consumer goods prices rose by 8.5% compared to the previous year and by a good 9% in the euro area in August. German producer prices shot up a good 37% in August 2022.

This has become possible mainly because – as I said earlier – central banks have created a huge monetary overhang. In the US, it is an estimated 15%, and in the euro area, it is of a similar magnitude.

As a rule of thumb, this means that goods prices will continue to increase at around this rate – in the sense that goods prices will increase by 15% in total, or by around 7% per year over the coming two years.

The increase in the money supply in the past and the resulting monetary overhang culminate in high inflation (which is bad enough), but not hyperinflation yet.

There is certainly no reason to give the all-clear, however. Because central banks' policies in recent years have made it unmistakably clear that printing new money is seen as the least evil in times of distress.

And this is unmistakably the attitude of inflationism, which promotes inflationary policies.

Inflationism becomes rampant at a time when the major economies of the world are heavily indebted, essentially over-leveraged, after decades of reckless fiat money expansion.

The coming hardships and political temptations can all too easily trigger ever more unchecked fiat money inflation, which, at some point, might become uncontrollable politically and eventually grow into hyperinflation.

Looking at it this way, one can say that high inflation is here to stay. Hyperinflation may not be at our doorstep just yet, but it is getting closer to our house every day – if the currently prevailing mentality on economic and socio-political matters does not change very soon, hyperinflation will come knocking – and eventually kick in the door.

While it is impossible to say when that might happen, in my opinion, the occurrence of hyperinflation in the fiat money system is very likely; in fact, I fear it is almost inevitable.

My advice to you is: Do not trust the official currencies US dollar, euro & Co. Adopt the working hypothesis that the purchasing power of the official currencies will be drastically debased, some even becoming a total loss.

Keep as little money as possible. It is best to reallocate amounts of money you do not need for current payments, such as time and savings deposits. For example, put them in physical gold and silver, in the form of coins and bars. And buy stocks (if you're not an expert, buy a world diversified stock market ETF or certificate).

And yes, there are other investment options, and greater investment portfolio diversification can also make sense. But investing in productive capital (i.e., stocks) and holding precious metals in physical form (i.e., as coins or bars) is an easy, viable, and inexpensive investment strategy for many people that will help at least partially escape the consequences of the ongoing and even accelerating destruction of the purchasing power of money.

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PRECIOUS METALS PRICES

In US-Dollar per ounce

	Gold		Silver		Platinum		Palladium	
I. Actual	**1689,6**		**19,5**		**907,8**		**2154,5**	
II. Gliding averages								
10 days	1713,8		18,4		859,4		2080,4	
20 days	1733,2		18,9		877,1		2089,0	
50 days	1742,8		19,3		886,2		2066,0	
100 days	1794,5		20,5		918,3		2035,8	
200 days	1834,1		22,2		961,1		2135,7	
III. Estimates for autumn 2023	**2200**		**28**		**1070**		**2261**	
(1)	*30*		*44*		*18*		*5*	
Band width	*Low*	*High*	*Low*	*High*	*Low*	*High*	*Low*	*High*
	1800	2398	21,0	31,0	830	1280	1650	2400
(1)	*7*	*42*	*8*	*59*	*-9*	*41*	*-23*	*11*
V. Annual averages								
2019	1382		16,1		862		1511	
2020	1753		20,2		878		2180	
2021	1804		25,5		1095		2422	

In Euro per ounce

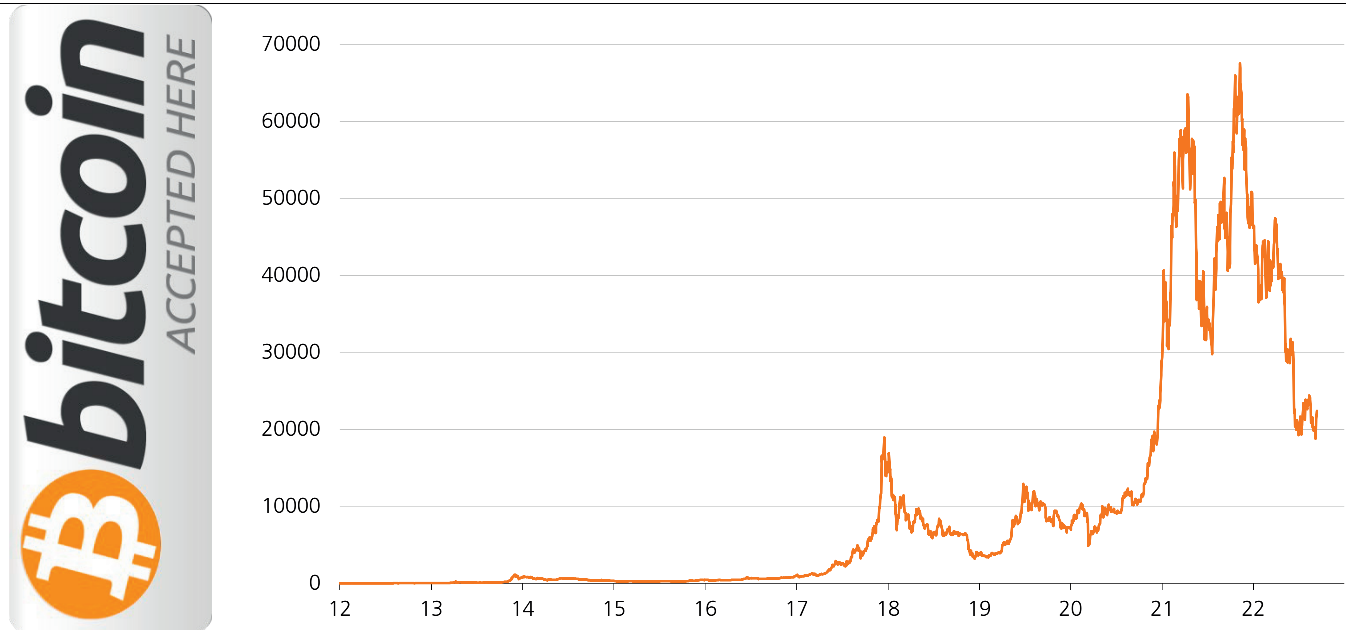
	Gold		Silver		Platinum		Palladium	
I. Actual	**1693,0**		**19,5**		**909,6**		**2158,8**	
II. Gliding averages								
10 days	1715,4		18,5		860,1		2082,0	
20 days	1730,2		18,8		875,4		2085,1	
50 days	1722,4		19,0		875,7		2041,9	
100 days	1735,0		19,8		887,6		1970,1	
200 days	1706,6		20,6		893,1		1987,1	
III. Estimates for autumn 2023	**2281**		**29**		**1110**		**2345**	
(1)	*35*		*49*		*22*		*9*	
Band width	*Low*	*High*	*Low*	*High*	*Low*	*High*	*Low*	*High*
	1867	2487	21,8	32,1	860	1320	1710	2480
(1)	*10*	*47*	*12*	*65*	*-5*	*45*	*-21*	*15*
V. Annual averages								
2019	1235		14		770		1350	
2020	1535		18		769		1911	
2021	1519		21		921		2035	

Source: Refinitiv; calculations and estimates Degussa. Numbers are rounded.

[(1)] On the basis of actual prices.

BITCOIN, PERFORMANCE OF VARIOUS ASSET CLASSES

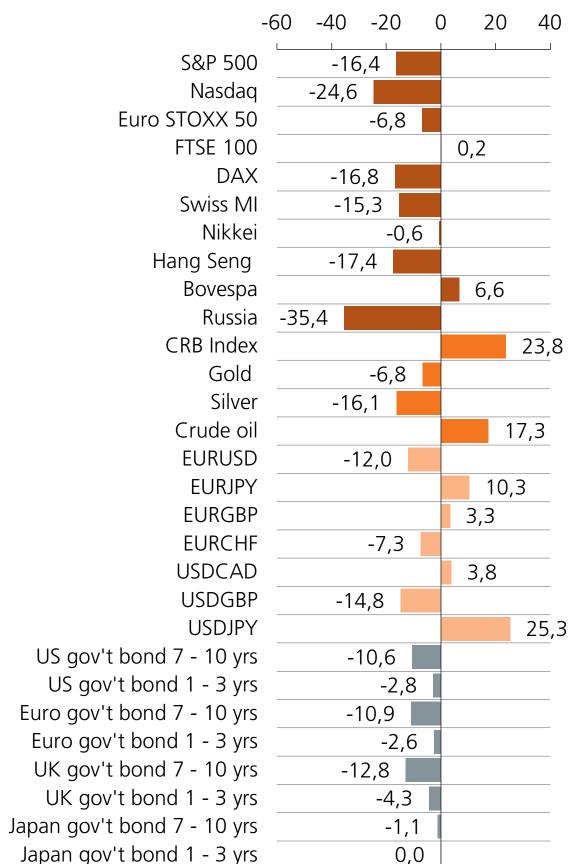
Bitcoin in US dollars



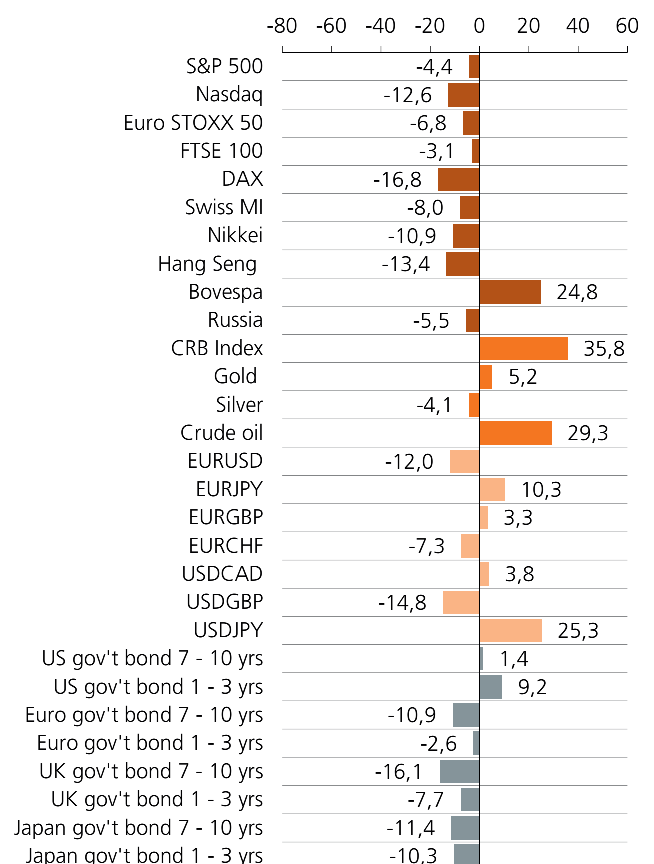
Source: Refinitiv; graph by Degussa.

Performance of stocks, commodities, FX and bonds

(a) In national currencies



(b) In euro



Source: Refinitiv; calculations by Degussa.

Articles in earlier issues of the *Degussa Market Report*

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1 September 2022	Everything You Wanted To Know About Money (But Were Afraid To Ask)
18 August 2022	Sky-High Inflation Is Just One Reason To Hold Physical Gold
4 August 2022	Excessive Money Growth Leads To Super-High Inflation
21 July 2022	Dollar Dominance Brings Yen And Euro To Their Knees
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17 February 2022	The Inflation beast is bigger than you think it is
3 February 2022	The Bigger Gold Picture
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21 October 2021	At A Crossroads. It Is Time For Gold And Silver
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12 August 2021	The Crime of 1971
29 July 2021	Gold And The Market Fear That Is Not
15 July 2021	Gold and the Monetary Policy Empire of Deception
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6 May 2021	The Dark Side of the Yield Curve Control Policy
22 April 2021	Bitcoin and the Golden Opportunity
8 April 2021	On Precious Metal 2021 Price Forecasts
25 March 2021	Money Matters For Gold And Silver Prices
11 March 2021	Interest Rates are to the Price of Gold What Gravity is to the Apple

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