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The British Pound

The Decline & Fall

By: Martin A. Armstrong
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World Economic Conferences

2012 Conferences

We will be holding three **World Economic Conferences** this year. These will be substantially different from the Philadelphia Conference. That was a combination of an **Analytical Training Seminar** and a **World Economic Conference**. Normally, each type of session is a two day event. Consequently, these two events had to be crammed into two days. Unfortunately, we could not accommodate everyone. We had to turn down 365 people. Traditionally, these events are limited to 100 attendees. Because of the overwhelming response, the room was full to capacity at 300+. That prohibited Mr. Armstrong from mingling with the crowd at the cocktail party and he was unable to see each and every person. These three upcoming conferences will be smaller, just forecasting, and will be two day events instead of the single day WEC which was provided in Philadelphia. Seating will be $1500 per seat. Those who are interested in attending please send your email to reserve a seat to:

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The British Pound

The Decline & Fall

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former Chairman of Princeton Economics International, Ltd.

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HE Decline & Fall of the Britsh pound has been a story of the Decline & Fall of an Empire that has followed the same identical pattern as all preceeding such declines and is the same pattern that once again the United States is following currently. There is not much that is different from the path of the decline of the British Empire than that of Rome or any other empire. The primary overall trend is first the concentration of capital within Britain that brings prosperity and raises that empire to the premier economic center that manifests in the ***Financial Capital of the World***.Once that has been achieved, investment tends to pour out of the center toward the peripheral economies as offering good value compared to the core ecnomy. This is largely caused by the concentration of capital accelerates inflation domestically. This results in rising property values, tangible assets, and of course labor costs. This makes labor cheaper with the peripheral economies and sets up an arbitrage that attracts capital from the core economy. This mechanism sets in motion the Decline & Fall for typically government becomes greedy and demands more and more revenue in taxes. This merely causes capital to further flee to the peripheral economies amd this accelerates the Decline & Fall of the core economy. Domestic labor inevitably becomes overpriced compared to the peripheral economies while consumers demand the best prices. The entire mechanism ensures the rise and fall of empires.

The British Pound "Sterling"

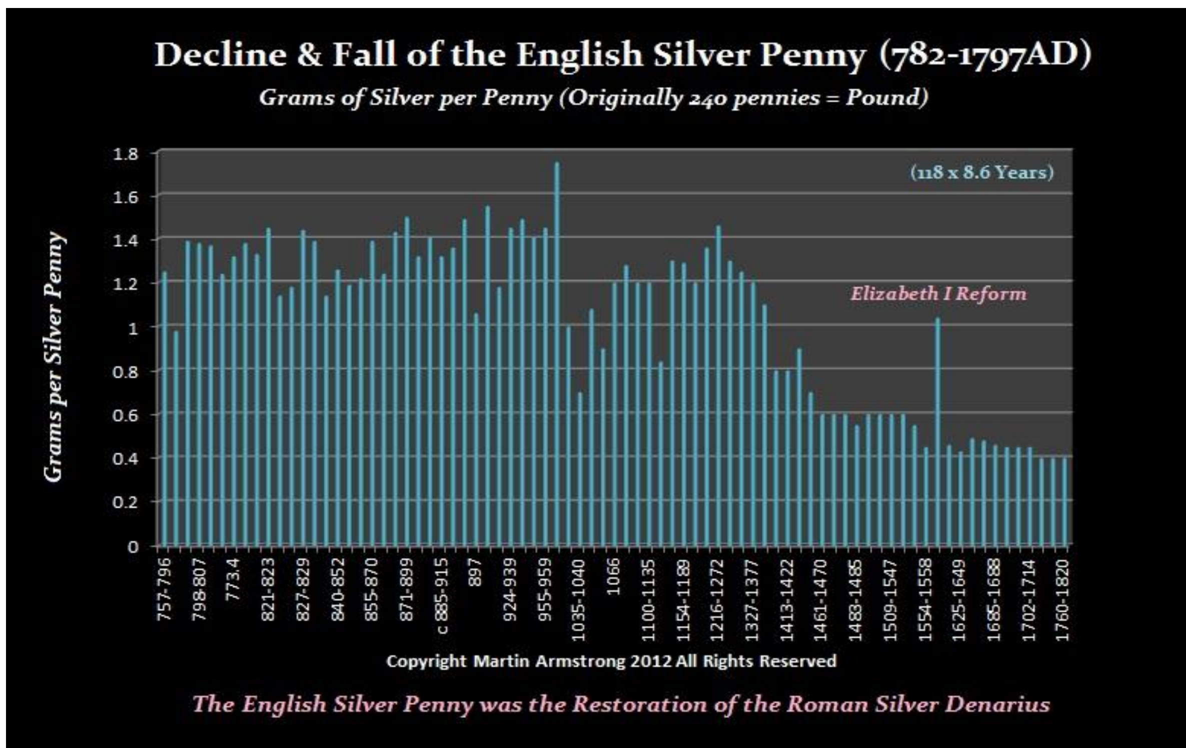
HE British pound after almost 300 years is still called "***sterling***" referring to its origin being one pound of coin silver .925 known as sterling silver. The first silver penny to be issued in England was that of the King of Mercia, Offa (757-796AD) who also issued coins depicting his wife Cynethryth in Roman tradition. His new monetary innovation was in part a restoration of the old Roman denarius that had effectively been wiped out by debasement during the 3rd century AD following a similar trend in France in 755AD there known as the denier. These silver pennies appeared around 782AD and were known as "***sterlings***" (silver pennies), which quickly became the main currency in Anglo-Saxon kingdoms. It is possible that they may have appeared as early as 775AD. Nonetheless, the weight of these silver pennies was such that 240 of them equaled one English pound, which was a tremendous fortune during the 8th century. A century and a half later, it was Athelstan, the first King of England as a whole, who founded a series of mints across his newborn unified nation that established the minting of coinage in England under the Statute of Greatley in 928AD instituting "***sterling***" as the national currency of the land. The term "***sterling***" was really slang for the first mention of the term "***sterilensis***" does not appear until 1078. The term was formally adopted by William the Conqueror, who introduced the "***shilling***" where 20 of these now equaled one pound of coin silver (.925). The term "***sterling***" thus became commonplace by the 13th century.

Its origins of the term "***sterling***" are lost to time. Stars and starlings both symbols appeared on the minted silver pennies, but no one knows if either gave their names to the currency "***sterling"***. The "***easterlings***", were early medieval merchants and moneychangers that came from the continent (east) and are another possible source of the name "***sterling***". Either way, the name stuck, linked to the meaning of "***ster***" in old German - strong, pure, stable, reliable, or excellent. English silver was held in esteem until the 16th century debasements. Nonetheless, the term "***sterling***" still remains with us today albeit no longer linked to silver or its origin whatsoever.

The English pound began as 240 silver pennies of about 1.3 grams approximately 782AD following the introduction of the silver Denier in France during 755AD by Pepin (751-768), which was the restoration of the ancient Roman denarius. In England, this new silver denomination replaced the Anglo-Saxon silver ***sceat***, which generally weighed 0.9-1.1 grams. It was under Offa, the king of Mercia, that the silver penny was introduced at about 1.3 grams on average complying with the French issues. No doubt, this was most likely influenced by trade for a ***sceat*** would be discounted due to its slightly reduced weight. By the time we reach Alfred the Great (871-899AD), these sterling pennies weigh on average 1.5 grams. Under Eadwig (955-959AD) the decline in weight of the penny unfolded with average specimens falling back to 1.25-1.4 grams. It is during the Late Anglo-Saxon Period of Edward the Martyr(897AD) that we begin to see the penny fall to 1.06 grams on average. Under Edward the Confessor (1042-1066AD), the silver penny falls below 1 gram initially with an average weight of .9 grams and then a drastic fall due to war dropping to .74 grams. With the French invasion, William I the Conqueror (1066-1087AD), the silver penny is restored to that of Offa's period - 1.3 grams.

Peppin (*the short*) (751-768) Silver Denier 1.3 grams

Anglo-Saxon Sceat *(7th-8th Century)*



Henry I (1100-1135) Silver Penny

Nothing lasts forever, and indeed, this is why there is no practical gold standard even remotely possible. People confuse the idea that gold is a recognized valuable medium of exchange with the idea that somehow gold is money that can be of a fixed value. There has always been an oscillating trend in the purchasing power of money regardless of what it might be. Karl Marx tried creating a flat line of value with Communism that attempted to eliminate this oscillation throughout history. He cost millions of lives and accomplished nothing lasting for the oscillation swings also eliminated Communism. At Christmas in 1124, a disgusted Henry I (1100-1135) summoned all those in charge of the mints (moneyers). They were called to account for the activities and he had 94 mint workers castrated for producing debased coins and pocketing the difference. Henry I was dealing with a monetary crisis in sterling value reflected in the chart above where even the weight collapsed from about 1.7 grams to just under 1.2 grams. This was a bloody public display amounting to an attempt to restore confidence in sterling pennies. However, during the civil war that followed his death, his daughter waging war to seek the throne issued coins at .84 grams. Once again, political uncertainty caused massive hoarding of the old coinage.

Matilda (*in England* 1139-1148)

This entire period is rich in its effects upon society long-term. This is when we find the famous "***Danse Macabre***" (Death Dance) as a result of the **Black Death**. It was seen as the great equalizer that was both impartial and inevitable. It became a period obsessed with death due to the nearly 50% mortality rate. This was merely enhanced by the **Hundred Year's War** (1337-1453) between England and France. This theme became popular in art that appeared in paintings, drawings, and cloisters of many monasteries. Thus, it was a series in which the whole hierarchy of church and state formed this stately dance where the living is escorted by skeletons who surprise them in the middle of their lives to escort them to the afterlife. This became a fantastic terror that strikes at the very heart of men. This was the impact of the **Black Death**.

Danse Macabre

The Peddler: woodcut designed by Hans Holbein, the Younger for the "Dance of Death" series, 1523-26

Economically, this drastic reduction in the work force instigated by the **Black Death** gave birth to independent labor and wages and the beginning of the end of serfdom and the Dark Ages. Land went uncultivated and landlords were now forced to pay wages to attract labor. This also had the effect of increasing the money supply relative to the population since the population was cut virtually in half. We have the same amount of coin available for half the population. This meant that the average person was indeed wealthier on an aggregate basis that caused inflation in itself. Yet the uncertainty of the period concerning death had the effect of also causing people to also hoard their wealth, especially in the face new rising of taxes. Therefore, we have the first peasant uprising over taxation in France during 1358. This is followed by a similar uprising against taxation in England led by ***Wat Tyler*** in 1381 that was a bloody affair.

The wars and uncertainty of the period caused the **VELOCITY** of money to drop and there begins to emerge a shortage of gold, for lack of circulation. In Paris in 1409, the foreign exchange brokers (*moneychangers*) rose up in protest that there was no gold available at any price. The civil war between 1411 and 1435, only further drove gold underground as it vanished from circulation. The French Crown issued an edict forbidding the manufacture of gold and silver objects to prevent the melting down of coinage to fashion into artifacts. They even tried to force gold out from hiding whereby at the port of Bruges, it was decreed in 1401 that all merchants had to settle accounts in gold. This was abandoned about 8 months later because it was impossible to comply with and merchants ignored it. The English output of coinage dropped by about 60% between 1476 and 1485, while the mints in the Flanders (Belgium) were even closed between 1402 and 1410.

Gold disappeared from circulation rapidly. This caused the economy to fall into barter once again. Just as cigarettes became money during World War II and in American prisons, the spice that was so valuable was pepper. This commodities became worth more than gold by weight and thus as bankers often emerged from merchants, this gave rise to bankers in Germany being called "***peppermen***". Thus, this period is often called the Great-Depression for money disappeared and commodities generally declined against the scarcity of gold. Wheat collapsed in price by about 50% between 1360 and 1500 because (1) there was a drastic reduction in the population reducing demand, and (2) the scarcity of precious metal rose in price due to its being hoarded.

Therefore, before we come to the Great Debasements of the 16th Century, this is the backdrop that must be understood. The price of gold rose consistently from 1350 when it was about 23 shillings an ounce to 40 shillings by 1500. Therefore, this entire period is extremely interesting because of the first **Sovereign Debt Defaults** of the 1340s, the **Black Death** that reduces the population on average by about 50%, which in turn leads to a decline in the primary domestic product of agriculture being grain (wheat/barley/rye) combined with the hoarding of gold causing the collapse in a circulating money supply. Talk about an economic perfect storm!

The first real regular gold coinage of England was that of Edward III (1327-1377). The first issue of 1344 was based upon the gold **Florin** of Florence where 6 shillings weighed 108 grains. This issue was replaced within a few months in1344 by the **Noble** with a weight of 138.46 grains valued at 6 shillings 8 pence, which was the equivalent of 80 pence, half a Mark or one third of an English pound. The third issue of gold coins in 1346 saw the **Noble** reduced to 128.59 grains. The fourth coinage in 1351 once again saw the **Noble** reduced in weight to 120 grains. The silver coinage during Edward's early years was issued in very small quantities. The debasement was clearly underway for by 1335 the halfpence and farthings, once produced at the sterling silver standard .925, fell to nearly 50%.

Henry VII (1485-1509) First One Pound Coin Issued 1489 in England known as the Sovereign 20 shillings (240 grains = 15.5517 grams)

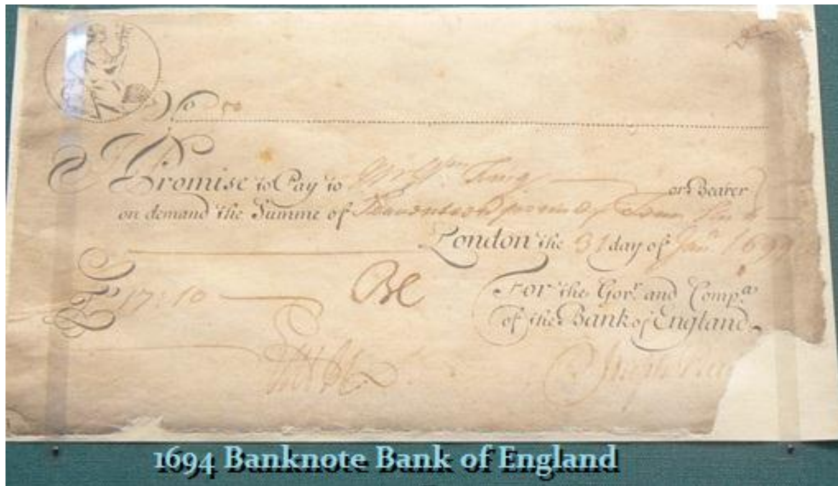
In 1489 Henry VII 1485 – 1509 made radical changes to coinage of England. The British pound sterling had never been an actual denomination of coinage just as the mark had been a unit of account on the continent. The pound was likewise merely an English unit of account for centuries prior with no coin being equal to one pound of silver. Now thanks to inflation we find the first 1 pound coin ever issued in England known as the "***Sovereign***" with a weight of 240 grains of gold or 15.5517 grams. Thus, a grain of gold is effectively one original silver penny at 1.3 grams when 240 pennies equaled one pound and now 240 grains of gold equaled one pound. This made the silver/gold ratio at that time about 20:1. Another innovation of Henry VII at this time was the introduction of the silver ***shilling*** known as the ***testoon***. Thus, the pound and the shilling as actual denominations rather than units of account began in 1489.

Henry VII (1485-1509) First Silver Shilling

Of course we have the Great Debasement of English coinage during the reign of Henry VIII (1509-1547). The fluctuations in the value of gold and silver between England and the continent played havoc upon the finances of Henry VIII. In 1526, the outflow of gold from England to France became critical. Gold as revalued upwards by 10% and the sovereign was raided from 20 shillings to 22 shillings. The gold coinage in England had always been minted at 23 carats. However, Henry VIII also lowered the fineness debasing the gold for the first time reducing it to 22 carats. The Sovereign was revalued at this time to 22 shilling, 6 pence.

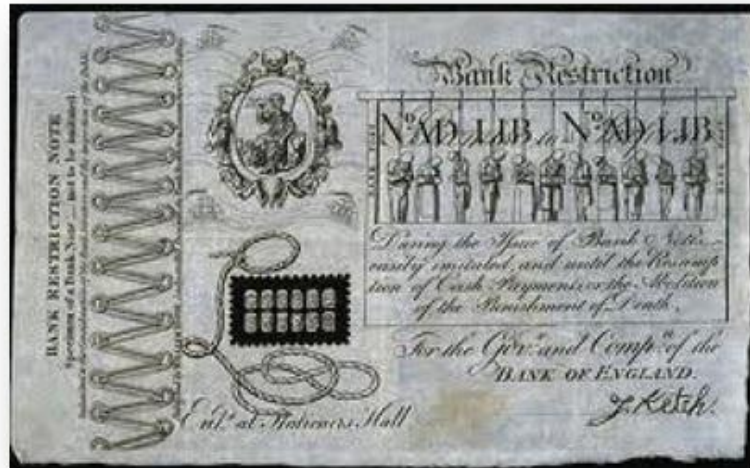
Wholesale debasement of the silver coinage began in 1544 and the right to mint coinage held by the Bishops at Canterbury, York, and Durham were not renewed. The debasement of the gold was 23 carat in 1544, 22 carat in 1545, and a sharp drop to 20 carat by 1546. The silver coinage debasement during this period was about 50%. Henry was effectively debasing the coins so that they would be largely copper with a silver plating. This earned him the nickname “***Old Coppernose***”.

Henry VIII was succeeded by his son Edward VI (1547-1549) who continued to debased coinage standard of his father. However, this debasement was causing massive economic problems and civil unrest. The VELCOITY of money was declining as the old coinage was no hoarded giving rise to Sir Thomas Gresham’s Law – bad money (debased) drives out good (undebased).As hoard soared, so did inflation as expressed in terms of the debased coinage. Finally, in 1549, the silver content was virtually doubled. Strangely enough, the higher silver content resulted in lighter weight coinage, which was still regarded as unacceptable. This resulted in a 25% reduction in silver content to increase the weight and “feel” of the coins. However, the shortage of cash led to further debasement and the silver dropped by 50% to its lowest level in 1551. This led to a whole new series of coins, the crown, half-crown, 6d and 3d all back at the full sterling standard. Mary (1553-1554) restored the silver coinage to to full sterling standard and struck all her gold at 23 carat. Elizabeth (1558-1603) recalled the debased coinage and countermarked it devaluing them in 1559. She minted silver at .916 and reduced the fineness and weight in 1601 by 1/32nd. She hung the moneyer Eloye Mestrelle in 1578 for counterfeiting. The Sovereign was now valued at 30 shillings, 1.5 pounds.



1694 Banknote Bank of England

Sterlings retained their importance throughout the middle ages. The Tower of London was the store for spare money. These silver pennies were the only coins right through until the 13th century and silver was the currency standard until 1717 when Britain adopted the gold standard as the basis for the pound. Nonetheless, it was in 1694 when King William III established the **Bank of England** to fund his fight with France. Goldsmiths had been issuing certificate of deposits (bank notes) with promises to pay set against gold deposits at least from the mid-16th century. Therefore, the idea of issuing bank notes against deposits was not new. It was convenient because otherwise moneychangers were necessary to certify the coins each time they changed hands. The money supply was plagued with counterfeits and clipped coins no less debased coinage. Bank notes became the practical means to conduct business for one need not certify the coins each time. Consequently, the Bank of England was emerging as an important innovation in economic development. Sterling banknotes were originally handwritten, although the notes were partially printed from 1725. Cashers still had to sign and make the notes out to someone. The Bank began to print the notes in 1855.



Bank Restriction Protest Note

However, by 1695 the first fraud took place. The authorities prosecuted Daniel Perrismore for forging sixty £100 notes. This incident caused the Bank of England to introduce a watermark in the paper to prevent such fraud. This was further enhanced by making counterfeiting subjected to the death penalty as a felony resulting in the confiscation of all your wealth throwing your family out of the street as well. Pictured here, is a protest imitation note. The law was being prosecuted on the mere possession of a forged note. The complaint here noted was that these one pound notes were easily forged and innocent people who were duped were being hanged with no proof that they created the forgery – merely that they possessed one. This was creating an incentive not to even accept the notes in transactions.

The Bank of England
the Old Lady of Threadneedle Street

It was the Irish playwright Richard Brinselyn Sheriden angrily described the Bank of England as "***an elderly lady in the city***". The name stuck. The Bank of England became known as the **Old Lady of Threadneedle Street**, nicknamed by the cartoonist James Gillray.

In 1708, the Bank of England received a generous gift from the British government. During a war with Louis XIV, Parliament restricted associations and banks of more than six individuals from engaging in banking business in England. This act essentially granted the Bank a monopoly over the issuing of bank notes; its only competitors afterward were small country banks of fewer than seven partners. Creditors were thus limited to storing their money at these small banks or with the Bank of England. The Bank regarded this monopoly over paper currency as essential to profitability, making concessions to the government as a way to protect and expand its control. The government, thus, had no problem with continuing to enforce the monopoly, because the Bank was a central figure in financing foreign wars.

In return for government support, the Bank continued to show its loyalty. In 1742, just before the Bank was due for rechartering, the Bank, not by coincidence, provided the government with an interest-free loan. The government expressed its gratitude by confirming its monopoly power, which reinforced the privilege of issuing bank notes, and extended its charter until 1764.

The Bank provided stability, but the pound still suffered from market ups and downs. The first £10 note was printed in 1759, when the **Seven Years War** caused severe gold shortages. In 1764, when it came time to extend the charter again, the Bank presented the government with a £110,000 gift on top of a cheap subsidized loan. The government gladly received another subsidized loan in 1781 in return for another extension of the Bank's charter until 1812. The government, as it was seen, needed the Bank's financing as much as the Bank needed the government's power of rechartering, special privileges, and authorization of the monopoly over issuing bank notes. Inflation fears of war with France led to the first £5 note in 1793.

The Bank Restriction Act of 1797 Legislation in the United Kingdom restricted the ability of the Bank of England from exchanging sterling notes for gold. At the time, the Bank of England was obligated to exchange the one pound sterling for one pound of gold on demand. However, the Napoleonic wars necessitated Parliament to order the printing of money to finance military operations. By 1814, 28.4

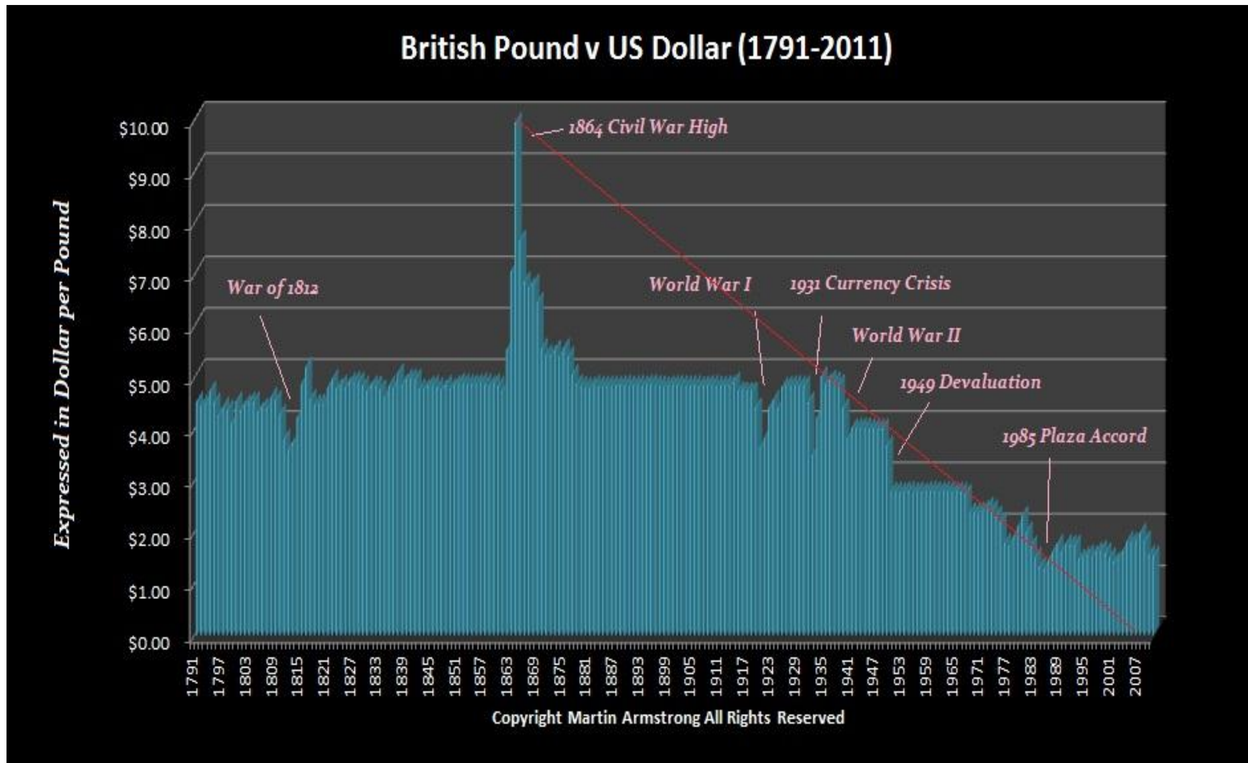
million pound notes were printed, but the Bank of England only held 2.2 million pounds in gold. This resulted in 30% depreciation for the sterling notes.

British involvement in the **Napoleonic Wars** followed the typical economic model – war results is inflation/depreciation in the purchasing power of the currency. By manipulating the currency and controlling the supply of money through the policies of William Pitt the Younger during the **Napoleonic Wars**, Parliament was able to satisfy its military ambitions with the aid of the Bank of England. The Suspension of Payments Act in 1797, played a critical role in wartime financial policy. Suspending payments of specie enabled the British government to fund its engagements abroad by inflating the currency and expanding the public debt, which was ultimately paid by acquiring funds through taxation. There was a series of runs on the bank in 1797, ushering in a period of fiscal restriction, which lasted until 1821. This is also when we find the extensive issue of bronze coinage under George III when Britain abandons the gold standard.

George III stopped minting gold coinage in 1799. He did not resume until 1813. Finally, in 1816, there was a major departure in the British monetary system. The gold coinage production was moved to Tower Hill and the finess was reduced to 22 carat (.916). The silver coinage of Britain fell well below its intrinsic value. Thus, coinage was taking on a fiat status whereby there was precious metal involved, but its value as official coinage was substantially higher than its metals content. Thus, the coinage became a form of "token" coinage rather than any precious metal coinage per se.

George III (1760-1820) Gold Guinea

(one pound)



The Gold Standard and Sterling's Supremacy

It was in 1717 when the British pound adopted the gold standard rather than its original silver foundation. Despite the distortion of history, there was no international "***gold standard***" until the 1870s when Germany finally adopted the ***gold standard*** that it became an actual world standard ushering in an era of grand scale international trade which lasted only until World War I. The downside of that development was of course competition that raised trade tensions that were released on the international stage of political intrigue and warfare culminating in World War I. The British Pound Sterling's strength was the based on the fact the Great Britain was the ***Financial Capital of the World.*** The ***gold standard*** thus gained its reputation only during this period for the rise of Britain. However, in truth, Britain was losing ground gradually and like Rome, it was too arrogant to take notice. Britain remained the ***Financial Capital of the World*** until it was also forced to abandon the ***gold standard*** in the face of World War I in 1914.

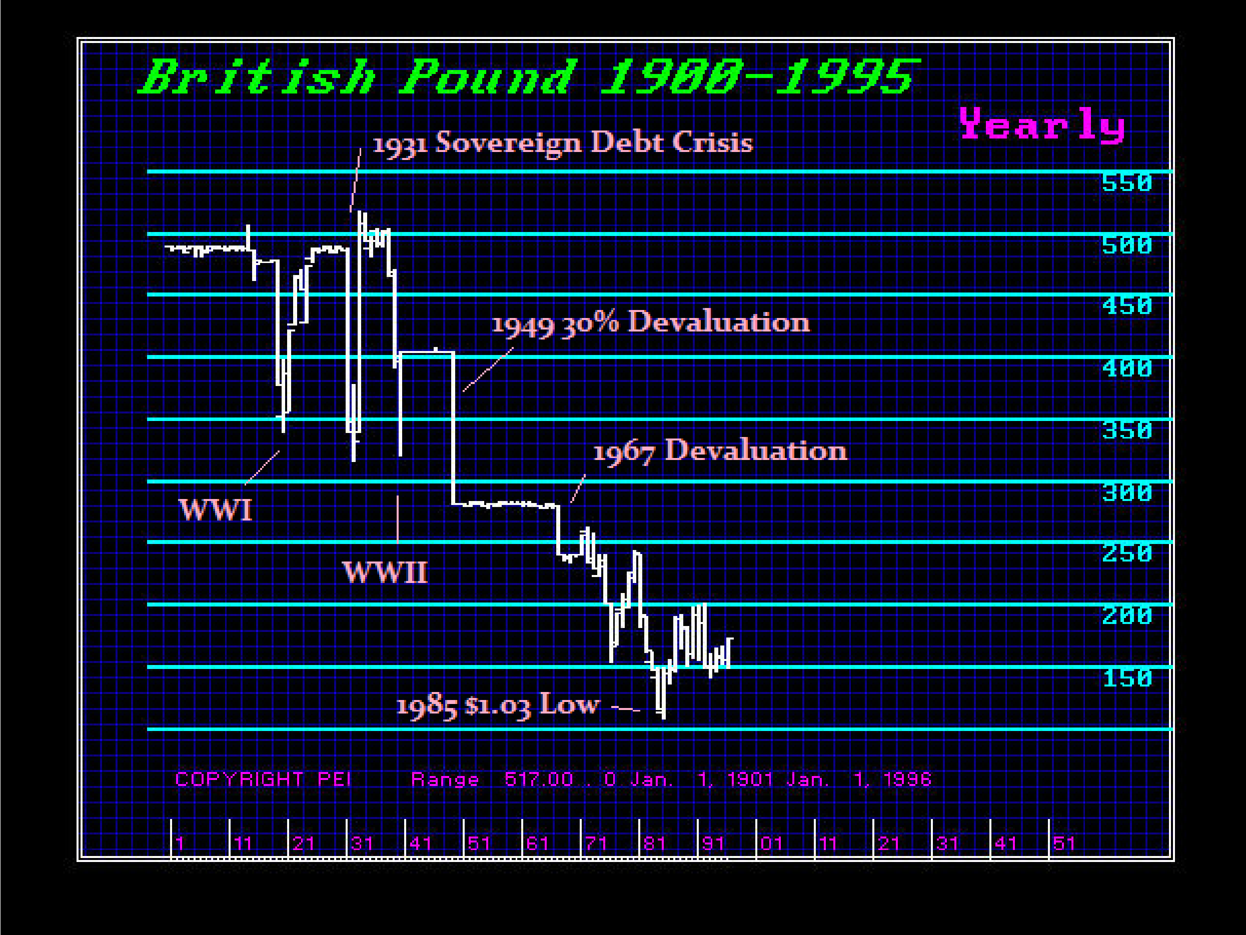
We can see here that the British pound remained quite steady from the birth of the United States until World War I with few exceptions being the Napoleonic Wars, War of 1812 with the United States, and the US Civil War when the dollar abandoned precious metals and adopted paper currency. In 1794, the exchange rate providing the number of dollars per British pound had risen to $4.75 versus $4.51 in 1793 showing there was an initial trend toward a "weaker" dollar. The dollar had depreciated (lost value) in comparison to the pound going into 1794, but it fell back to $4.13 into 1799 forming the first 5 year bear market for the pound. The dollar declined as the pound rose to $4.63 in 1808 but then collapsed to $3.62 during the War of 1812. The dollar then collapsed and the pound rose to $5.22 going into 1816, a

level that was not exceeded until the American Civil War in 1862 as the dollar collapsed driving the pound up to $9.97 for 1864.

The idea that there can be any standard involving money is clearly erroneous insofar as establishing a fixed value for money. That implies that there will be no oscillation in prices of various markets. For real estate to rise in price means the currency value must decline. This notion of fixing a standard is separate and distinct from the idea that all nations recognize that gold is a medium of exchange. The price of gold simply oscillates rather than remaining fixed. This is further separate and distinct from issuing banknotes by a bank or paper currency issued by a monetary authority. The former was supposed to be a one for one receipt whereas the latter tends to reflect the national capacity to produce on a collective basis. Sterling's strength during the 18th and 19th centuries was not the basis of the ***gold standard***, but of the rise of Britain to become the Financial Capital of the World after William III brought Dutch ways of finance and business to Britain when he took the throne in 1688. The great period of global imperialism for Britain also ushered in the great period of diversity in global investment. British investors poured money into offshore investments, instigated by the strength of sterling and the might of the trade wealth of the British Empire. Britannia indeed ruled the waves, and sterling was the global economy's reserve currency. However, the capital outflow from Britain eventually drained its domestic economy in the long run because of its unavailability for the local British industry and the rise in British labor costs. This trend of rising domestic labor costs instigated by the rise in the wealth of the nation then contributed to a lengthy and slow decline in sterling's face value to the point of collapsing to virtually par against the dollar in 1985.

William III of Orange
(1650; English King 1688-1702)

World War I put an end to not just the British the ***gold standard*** in 1914 under the to the necessaries of escalating war expenditure, but this also market the peak in the British economy as the Financial Capital of the World. After the war Britain sought to return to its former pre-eminence, ignoring the consequences of the war returning sterling to the ***gold standard*** in 1925 at the pre-war rate of £4.86 to the dollar. However, the pound was clearly overvalued by 10 to 20 per cent. The rate of exchange for sterling had been unchanged since Sir Isaac Newton set it in the 18th century, when he was Master of the Mint. The value was very out of date with reality and the loss of economic power. The labor unions became much more militant after the War and this merely accelerated the economic decline thanks to the usurpation of democratic free market trends that further weakened the pound. The Marxist agenda of creating a social class draining the productive forces set in motion the gradual slow economic decay.



The dollar's growing dominance began to reduce sterling's importance as a reserve currency, while sterling remained overvalued. By the end of 1925 the economics of the coal industry had collapsed, and 1926 brought not stability, but a six-month coal strike, the general strike, and long-drawn-out unemployment. The rising labor disputes culminated in the **Sovereign Default Crisis** in 1931, that effectively ended the Gold Standard as nation after nation defaulted on its national debts. Britain entered a moratorium on its debt and eventually resumed payments.

World War II saw a prodigious increase in forgery, as Germany's Nazi government sought to weaken sterling by spreading counterfeit notes. By 1943 the Germans were producing 500,000 banknotes a month and, although the majority were seized by the allied forces and were destroyed, for years after the war fake British pounds were causing major headaches for the Bank of England. To counter the fraud, the Bank introduced the metal thread during the war to differentiate its issue from the German forgeries and ceased producing some of the higher denomination notes altogether.

The **Bretton Woods** conference in 1944 heralded the end of sterling's predominance in international trade shifting the status of the reserve currency to the American dollar as the United States end up with 76% of the official world gold reserves by the end of the war. The **Bretton Woods** agreement defined both the dollar and the pound as reserve currencies at first, which was deep blow to the British pride.

That reserve status of the dollar and the pound meant that other nations must accept dollars or pounds to settle debts. However, each country, including Britain, would define the value of its currency in terms of dollars, while the U.S. would tie the value of the dollar to gold stupidly fixing the rate at $35 per ounce. This would eventually lead to economic chaos in the mid to late 1960s and the collapse of the **Bretton Woods** gold standard by 1971 as the supply of dollars increased as the supply of gold decreased. Yet politicians will never admit a mistake and instead of readjusting the gold price upward (devaluing the dollar), this led to the entire collapse of the gold standard in 1971.

Bretton Woods Monetary Conference

The British pound was simply never a popular reserve currency post-World War II, although the Commonwealth sterling block helped it retain some importance within the currency markets. Nonetheless, the rising socialism in Britain led to many rumors that sterling would be devalued, and as such many countries converted their pounds to dollars declining to hold the pound as a reserve currency. That expectation proved to be correct for by 1949 sterling's importance as a reserve currency collapsed. Sir Stafford Cripps, then Chancellor of the Exchequer, denied the obvious in public. Yet the pound was devalued by 30% on September 18th, 1949. The enormous postwar balance of payments deficit was just too much for the Britain to sustain and they were forced to devalue the pound. The pound was no longer regarded as a safe reserve currency.

The British obsession with maintaining sterling's role as a reserve currency led to the politicians keeping the pound overvalued. This made British exports uncompetitive within the commonwealth and contributed to the economic decline in the face of rising labor disputes. In 1967 the Labour Prime Minister, Harold Wilson, and his Chancellor of the Exchequer, James Callaghan, devalued the currency again, this time by 14.3% trying to deal with the uncompetitive value of the pound. It was at this time that Harold Wilson made his famous "***pound in your pocket***" speech, in an attempt to reassure the public about their wages. Nevertheless, life did become more expensive as the devaluation led to inflation as exports increased in cost. Where the massive 30% devaluation of the pound in 1949 stimulated British exports, the 1967 devalue was not enough and amounted to too little too late. Inflation rose, but British exports declined.

The British Empire crumbled as the sterling currency block cascaded towards lesser importance and the pound's devaluation in 1967 portended the end of the **Bretton Woods** system of fixed exchange rates was on the horizon. The pressure on the **Bretton Woods** gold standard were clearly mounting and this forced the first break with gold moving to a two tier system in 1968 and the birth of the London gold

market. Now gold would have a two tier pricing structure – a free market price and the official price among nations that was still fixed at $35 per ounce.

Nixon closes Gold Window
August 15th, 1971

But on **August 15th, 1971** President Nixon devalued the dollar after the French and the Swiss were demanding gold for their dollar reserves in the face of massive dollar expenditures for the Vietnam War. The stability of a gold standard proved fatal as the idea of fixing the value of money was simply futile in the face of political objectives.

The closing of the gold window was to be merely a temporary measure subject to negotiation. Nonetheless, Watergate, War in the Middle East, high oil prices and an international recession, all combined to ensure the birth of the Floating Echage Rate System. From the British perspective, the rising socialistic labor trend combined with the slow economic decline sending Britain into an economic tailspin. By 1975, in the face of inflation and a large scale coal miners' strike, the Britain was forced to apply for a loan from the International Monetary Fund. This struck deeply at British pride and set the stage for the election of the first woman head of state – Margaret Thatcher.

The turmoil of the period set in motion the first tentative steps towards a European currency in 1972 as Europe sought to reestablish a fixed exchange rate system among its member states. These efforts to fix the pound to other European currencies would set the stage for a much later crisis in 1992. Hence, the four major European Economic Community [EEC] currencies - sterling, the deutschemark, the French franc and the Italian lira - formed the so-called "***snake"***. This economic union floated their currencies together on the markets, yet each country retained responsibility for the stability of its currency within the established parameters. This allowed for some fluctuation but between a maximum and minimum band – thus the term "***snake***" was born. Failing to comprehend the nature of free markets, the experiment of course failed rather quickly. Sterling was unable to remain within the bank and was forced to drop out after only six weeks. The pound was now weaker than ever trying to buck the free markets that simply have little confidence in its Marxist driven goals. While labor kept trying to freeze the free markets to force trends to support unrealistic labor policies, the pound simply lack international confidence and this ensured that the currency markets were just too volatile to fix the exchange rates together without damaging the British economy creating an economic depression.

By 1976, the pound fell below $2 for the first time. The government approached the International Monetary Fund [IMF] to shore up sterling's value. The politicians were in disarray. They failed to understand economics and saw the decline in the pound as an embarrassment regarding their policies. Rather than address the economic problems, they naturally sough loans to artificially support the currency. The new IMF loan included a "***letter of intent***", which was a humiliating agreement to pursue

stable economic policies. This allowed the pound to gather some strength. The pound had fallen from $2.64 in the first quarter of 1972 to the fourth quarter 1976 where hit collapsed to $1.57. This had been a devastating blow to British pride. The pound rallied to $2.45 into the fourth quarter 1980. By the end of 1977 the British government had abandoned efforts to keep the pound within the trade weighted index. Sterling was on the rise and the devastating policies of the Labour Government set in motion the election of Margaret Thatcher came to power on the 3 May 3rd, 1979 election and she became the longest-serving Prime Minister and the first woman to hold that position (1979–1990). In 1975 Thatcher defeated Heath in the Conservative Party leadership election and became Leader of the Opposition, as well as the first woman to head a major political party in Britain.

Upon becoming the Prime Minister occupying 10 Downing Street, Lady Thatcher introduced a series of political and economic initiatives to reverse what she perceived as a precipitous national decline in Britain that had followed closely the path of Marxism. Her political philosophy and economic policies emphasized deregulation of the financial sector that set in motion a resurgence of Britain in world financial circles. She also pursued flexible labor markets and the privatization of state-owned companies, which was a direct attack upon Marxism. She also sought to reduce the power and influence of trade unions.

Lady Thatcher's popularity waned amid recession and high unemployment as labor naturally took the position that capital could be regulated into submission. Finally, an economic recovery began in 1982 and the 1982 Falklands War brought a resurgence of her support and British pride. This helped her win re-election in 1983. Thatcher was re-elected for a third term in 1987, but her policy that there should be a Poll Tax proved highly unpopular. She felt that the bulk of the people were not paying anything toward government and were just receiving benefits. This, she believed, divested them of a shared view of the benefit of the nation and merely set up a confrontational self-interest role within society.

Lady Thatcher was also skeptical of the European Community contrary to her Cabinet. Eventually, her ideas became the majority keeping the British out of the Euro. Britain was then in the EU, yet out of the Euro. She resigned as Prime Minister and party leader in November 1990, after Michael Heseltine launched a challenge to her leadership.

The collapse of the pound to $1.03 in 1985 was not seen as a reflection of Lady Thatcher's policies since this was a broad-based rally in the dollar. This led to the ***Plaza Accord*** and the formation of the G5 in 1985 to once again force the free market6s to do what the politicians though should take place. Central banks around the world intervened to prevent the dollar becoming too strong and by 1987 the dollar was at what bankers saw as the 'correct' value - so decided at the ***Louvre Accord***.

Nigel Lawson was Lady Thatcher's Chancellor at the time. He decided to cap the pound against the deutschemark, inspired by the growing European integration. The pound would not exceed three deutschemarks. Lawson believed by fixing the pound and deutschemark, would bring Britain's competitive and inflationary pressures into line with Germany. But Europe at the time was growing slower than the UK, a condition then known as ***eurosclerosis*** due to the fact that continental Europe had not made the dramatic privatization moves that Britain had accomplished under Lady Thatcher. The result was massive capital inflow to Britain. Sterling rose as investment flooded in as capital saw Britain as the new place to be.

Lawson had to abandon his cap, but by then it was too late. Inflationary pressures had taken off spurred by massive capital inflows that increased domestic money supply. This was also contributed by the fall in 1985 of the pound to $1.03 US that then suddenly attracted massive capital inflows from US investors. Property markets in Britain soared after domestic investor believed prices were already too high. These trend cause consumer spending to rise with property values and a wholesale boom was underway. To rein in these pressures interest rates were increased. The cycle turned down in 1989 as both the property market and consumer spending collapsed. This led to the shift in political fortune for Margaret Thatcher.

Black Wednesday - September 17th, 1992

Lawson's successor at 11 Downing Street was John Major whose policy was to reduce UK interest rates and thus revive of the British economy. It was Major who decided to join the **Exchange Rate Mechanism** (ERM). Interest rates in Europe were much lower than in Britain. Major entered the ERM with the pound fixed at £1 to 2.95 deutschemarks, which was effectively about Lawson's old cap. Major was hoping for revitalize inflation to end the deflationary trend created by the high interest rates, which was opposite of Lawson's objectives. The ERM rules dictated that the pound was to vary by no more than 6% from its entry rate making the swing no more than 3% either side of the ERM official rate. The idea was to reduce British interest rates of 15% by linking them to Germany's 8%.

Nevertheless, the deutschemark strengthened against the dollar between 1989 and continued into the second quarter of 1995 as did the Japanese yen. This was ***die Wende*** (The Turning Point) that marked the process of German Unification. Between 1990 and 1995, gross wages in the east rose from 35% to 74% of western levels, while pensions rose from 40% to 79%. October 3rd, 1990 was the official Unification day. On 15th of March 1991, the Treaty on the Final Settlement with Respect to Germany entered into force, putting an end to the remaining limitations on German sovereignty that resulted from the post WWII arrangements. Therefore, this was the precise wrong time for the pound to attempt to be link with the deutschemark.

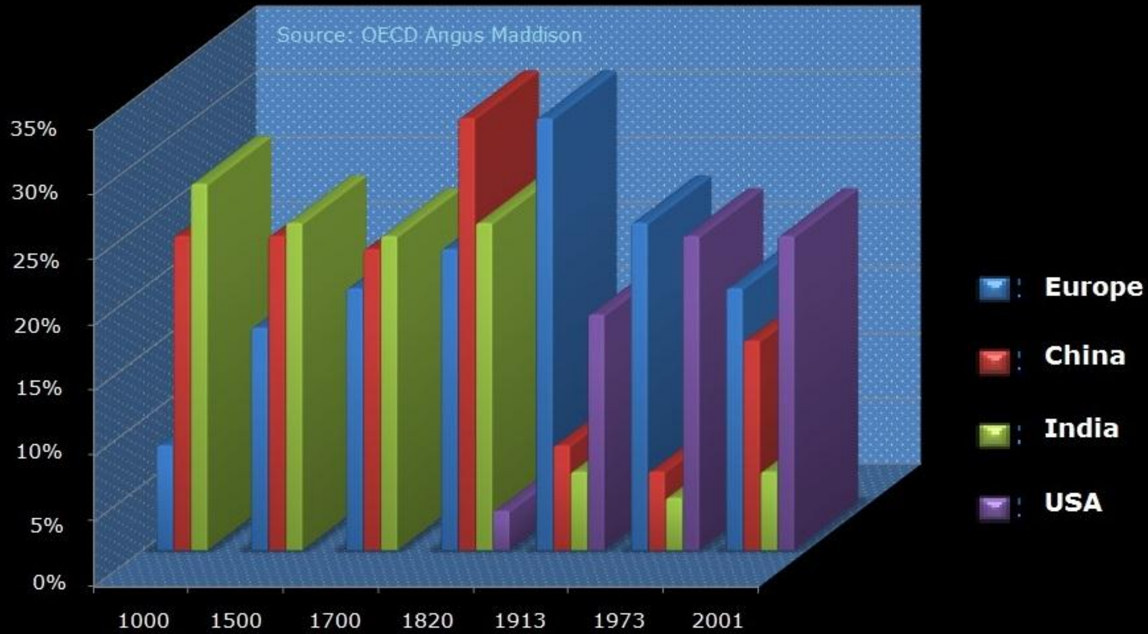
The pound peaked at $2.01 during the third quarter of 1992, and then crashed into the first quarter of 1993 falling to $1.41. Germany boomed and the UK slipped further into recession as the expectation for Germany skyrocketed with optimism. The fixed strength of sterling, maintained within the ERM's limits, caused British exports to decline. Major government's made desperate overtures to the Bundesbank to

lower interest rates and so weaken the deutschemark were counter to the fear of domestic inflation in Germany. The two nations were now diametrically moving in opposite directions. At the Bath meeting of European financial ministers in 1992, the differences in philosophy between Britain and Germany were exposed for the world to see. At the summit Norman Lamont, Major's successor as Chancellor of the Exchequer, harangued the Germans over their interest rate policy that was causing deflation in Britain thanks to the ERM. It was at this time that hedge funds, led by George Soros, could see that the political policies between Germany and Britain would force a break of the fixed ERM between the two currencies. Sterling was overvalued relative to the deutschemark and something just had to give. Fixing currencies proved to be a fantastic trade. If one was wrong, there was no downside since governments were guaranteeing the peg. If traders were correct, then they had tremendous upside by shorting the pound and negligible risk.

On **September 17th, 1992**, the Chancellor, Norman Lamont, announced that the Government could no longer hold the line at the end of a day of desperate and futile attempts at propping up sterling, which included spending what the City estimated as £10 billion from Britain's reserves and a two-stage rise in interest rates to 15 per cent. Mr. Lamont later rescinded the second rise, and said interest rates would be pegged at 12 per cent, two points above the rate on the previous night. The announcement sent sterling tumbling in New York trading last night, hitting DM2.69 - nine pfennigs below its former permitted ERM floor against the German mark. He shifted exchange rates up from 12 per cent to 15 per cent on that one day, but his attempts to support the currency came to nothing. The pound devalued and Mr. Soros, who was rumored to have made as much as $2 billion in his bet against sterling, was christened "***the man who broke the Bank of England***" by the Daily Mail. That day became known as **Black Wednesday** boosting the ***Eurosceptics*** that would eventually help to keep the pound out of the Euro. John Major remarked afterwards: "***It was a disaster, a political disaster, there is no doubt about that. It was an embarrassment for the United Kingdom.***"

Since that fateful day in 1992, the British pound has remained a free floating currency – the longest running currency in history. The idea of a fixed exchange rate system orchestrated by politicians for political purposes has proven to be one of the worst possible monetary systems. Money simply cannot be fixed. It is the equivalent of a national stock and its value will rise and fall depending upon the confidence the world has at that moment within that particular economy. Officially, in October 1992 this target range within the **ERM** was initially set at zero to four per cent, but later revised to 2.5 per cent with a one per cent band on either side by Tony Blair's New Labour government. Of course, whenever the currency is out of line with the free markets, the latter will dictate its value, not political will.

The history of the pound and the attempt to establish fixed exchange rates within Europe post-1971, demonstrate that no such standards are ever possible. Money, regardless of it might be, will fluctuate in value for it must do so or else we end up with the Communistic model that simply collapses. Nothing would rise and fall in price if everything were fixed. When politicians seek to create fixed exchange rates, what they create is an economic nightmare for they are unable to manage an economy dispassionately. Currency exchange rates have been played with solely for political purposes and therein lies the disaster.



THE FRACTAL CONCLUSION

The core pattern here of how nations rise and fall is the same pattern we see in all market activity and the concentration of wealth. This is why Marxism has caused such a nightmare and why we now face a Sovereign Debt Crisis of untold proportion. Capital will always concentrate be it on an individual level into the hands of the most industrious, within a single market segment that creates the boom-bust cycle as was the case in the DOT.COM Bubble, Russia, China, Japan, or countless other cycles such as the USA in 1929. Yet the rise of one nation above another is the same process as capital concentrating in the hands of the most industrious.

Marx was extremely jealous of wealth. He saw the natural process of economic development as evil. Some people are vegetarians yet turn on a nature show and you will see a lion ripping the throat out of a zebra. Life was designed where one species feeds upon another. The design may be offensive to many. But it is the design that we cannot change as a whole. We can choose to participate or not, but we cannot pass a law and forbid others from doing what we find offensive.

If you look closely at the development of real estate cycles, you will see that prices first begin to rise in the core city. It spreads gradually from there outwardly until it reaches the suburbs. By the time it

reaches the peripheral regions, the first core section is already starting to decline. This is the same pattern by which the rise and fall of nations follow. As capital concentrates within a nation, such as it did in Britain, it causes labor prices to rise becoming uncompetitive relative to the outlying regions. Labor then becomes greedy and instead of improving skills to warrant more money, they simply demand more money for the same job. That causes the outflow of capital as does the rise in taxation.

Eventually, capital flows out from the core economy and moves into the peripheral economies. This was the same pattern that took place in Greece, Rome, Britain, and now the United States. Government cannot regulate this natural flow bucking the trend. The failure to understand the trend and how it functions leads only to financial crisis created by artificial means of trying to suppress it.

This is why there is no empire, nation, or city state that has ever survived and retained that title of the ***Financial Capital of the World***. This is why we are going through major economic changes and politicians are incapable to dealing with these issues because they are more concerned about retaining power and promising things people want to hear rather than telling them what the need to hear. Thus, no one has held that title forever as illustrated here of the movement of the ***Financial Capital of the World.***

The World Share Market Outlook for 2012

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