**Roubini: Here's Why a Gold Standard Won't Work**

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A gold standard would just make business cycles more extreme, according economist Nouriel Roubini.

What's more, a gold standard would make central banks unable to fight inflation or deflation, much less do anything to combat persistent unemployement, Roubini said in an interview with NetNet yesterday.

"A fixed exchange regime, even if it is not a gold standard... That world just doesn't work. Because in that world, monetary policy by definition instead of being countercyclical becomes procyclical," Roubini told NetNet. "Suppose you have a fixed exchange rate regime...It just exacerbates the business cycle."

Roubini asks us to imagine two countries: One that's growing very quickly, and one that's growing very slowly.

The economy that is growing quickly would tend to "overheat"-an economic phenomenon characterized by accelerated growth, inflation, and the potential for asset bubbles. In the economy that is growing more slowly, there would be a tendency toward deflationary pressure and recession. So, instead of having a central bank with the capacity to successfully counter-balance these tendencies, an economy fixed exchange rate regime is to continue to reinforce the existing negative trends in the business cycle, Roubini argues.

Although he is best known as an economist who challenges conventional views, Roubini pretty well lines-up the consensus view of mainstream economics on the gold standard or fixed exchange rate regimes: "You have the opposite of what any optimal rule about monetary policy will tell you."

The ranks of the gold standard advocates, which have long included many Austrian economists and others worried about central bank manipulation of the money supply, were seemingly joined this week by World Bank President Robert Zoellick. Hardcore gold standard folks, however, are skeptical of Zoellick.

Nouriel Roubini agrees with the skeptics. "In fairness to him [Zoellick], he was speaking about a wide variety of issues in the global economy... So it was not a proposal centered around going back to some modified gold standard," Roubini said.

Roubini seems to think a gold standard is a pretty awful idea. "There are many fundamental problems with any variant of a gold standard," he said.

A general summary of Roubini's position on the issue would likely begin by saying that, generally speaking, a fixed exchange rate regime or gold standard limits the flexibility and range of actions that central banks can take to improve a nation's economy in fundamental ways. (For example, in a fixed exchange rate regime, central banks have less ability to maximize employment, stimulate growth, and manage price stability.) And, as Roubini specifically pointed out to me, fixed rate regimes inhibit the ability of banks to provide lender of last resort support to an economy when necessary.

According to Roubini, there are other major feasibility issues with the proposals for a transition to a global gold standard. One of the principal problems with such proposals is the current level of central banks' gold reserves.

Roubini raises the following question: If you are on a gold standard, or modified gold standard, what do you do in the event of a bank run-if you don't have enough gold to fully back the currency? Roubini explains that most central banks in today's economy have far greater financial liabilities than gold in reserve. In fact, according to Roubini, in the case of most central banks today that ratio is about 40 or 50 to 1.

Of course, many who support a gold standard would say that limiting the ability of central banks to increase their leverage would be a benefit of adopting the gold standard.

Aside from the issue of central banks insufficient current gold reserves, there are the issues that historically plagued gold standard economies. One of the most intractable of those issues was the impact that the gold standard had on traditional business cycles.

Historically speaking, Roubini says, during the days of the gold standard economies were constantly imperiled by spasmodic cycles: "When you had a traditional gold standard, boom and bust with severe swings in economic activity were the norm-really big ones. It was only once we moved to fiat money that central banks were able to smooth the business cycle, and make it less volatile, as we did during the financial economic crisis."

Of course, this directly contradicts Austrian business cycle theory, which argues that boom-bust cycles are caused by central banks departing from the gold standard.

In short, Roubini views challenge the Austrian economists where they live: at the intersection of monetary policy and the business cycle.

We eagerly await the response. Over to you Ron Paul and the Mises Institute!

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I have to laugh when people say gold and silver are investments that don't generate cash. So, that money you have sitting in the bank, losing purchasing power every day, earning next to nothing in interest, IS generating cash? I agree with the posters suggesting that you put yourself on your own gold standard. The world is waking up to the trapped box the Fed has put itself in. Interest rates can not rise, the interest payments on the stifling debt would go through the roof and choke off what is left of the economy. So, those with assets are choosing to leave the paper system in droves and put that cash to work in hard assets, farm land, stocks of companies that own real assets and have real businesses, real income producing real estate, etc. You see, when you have assets, you like to generate a return on those assets--you like to have them working for you increasing your wealth. Paper isn't paying anything, and it looks like it won't for a very long time unless you want to go way out on the risk curve. I'll choose real things, thank you.

The real problem Roubini sees is that it will preclude the manipulation of the markets by his partner, the FED. You can't print unlimited money when it has to be backed by a tangible commodity.

A gold standard or even a variant [gold, silver, platinum, Rare earth minerals] is a healthy alternative to dollars revalued like rubles or pesos, despite the setbacks it may create.

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what makes gold the end all commodity for propping up the economy..when the crap hits the fan, you can't eat it...it won't keep you warm...in theory it could be worth so much less as it was only a few years ago... institutions and the uber rich can force market and economic cycles by trading it..why is it so much more secure than say platinum or titanium?

I'm surprised to hear Roubini say something so stupid. His entire scenario he presents makes no sense at all. If central banks aren't manipulating the currency then the market decides what the interest rates are based on how much free capital there is!! That's precisely what prevents bubbles. I'm sure you could still have over borrowing or over saving simply from people making bad investment choices but the entire market itself won't be thrown own by money printing and rate manipulation.   
  
And if central banks don't have enough gold then they should consider buying more!!! More would be available for them to buy if they issued a gold backed currency so people could trust the currency rather than having to buy gold themselves. His entire thought process is just so bogus I'm shocked.

Well, it's good to see that Austria - that economic powerhouse in the world, has something to offer other than skiing and chocolate. After all, doesn't the G20 consult the Austrian government every time it considers making a policy move? They don't? You mean they only produce skiing and chocolate? Oh, sorry, I got them mixed up with that country next door - Swiss-er-land.

I guess it's time for that bozo thinks he needs some explosure again. Yes, Mr. Roubini, when you said there were 50% chance the economy would tank again, you know you are playing the probability game. There is only up or down in stock market, so either way, you statement is always correct. Use some solid numbers to back up your claim next time.

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