An EMS link for the dollar?

The recent price fall may represent a move toward President Reagan's real gold price.

The recent sharp drop in the price of gold below the $500 an ounce barrier for the first time since May 1980 is being played by London traders as a bottomless pit. Many an American investor has been frightened of late by London traders' talk that the price may plummet to $400 or worse, and that all is uncertainty.

True, a great deal of the selling wave was touched off by the British. Major London firms began dumping gold out of Hong Kong early on the morning of Jan. 26, after David Marsh, the London *Financial Times* gold columnist, reported a selloff of gold by Hong Kong, Singapore, and Mideast investors. Since then, London traders have also insisted that the Iranian central bank is dumping physical gold every time the market moves above $500 per ounce.

But, in fact, the continental European central banks, led by Germany, France, and Switzerland, are in the market, well-connected Zürich sources say. They have established a price support area, in which they will buy, of between $450 and $500. It will be recalled that the Swiss National Bank late last year announced that it will be buying gold for its own account, and the Swiss are not fools enough to buy straight into a price collapse.

Rumors of Far East, Mideast, and Iranian gold dumping are furthermore "ridiculous," say these same sources.

It may be instead that President Ronald Reagan's stated desire to return the United States to the gold standard is an active topic of consideration between the Reagan administration and the leaders of the European Monetary System. It was "increasing talk about returning the U.S. to the gold standard" which revived gold this week, say traders in Geneva.

It is no secret that President Reagan has told Federal Reserve Board Chairman Paul Volcker that he would like to see gold "closer to" the four hundreds price. It has been calculated, Washington sources say, that there is a "real price" of gold which represents the actual cost of production of an ounce of gold from an American-style mechanized mine. Accounting for high-technology mining capital investment and American-style wage levels, the "real price" today would be slightly over $450 an ounce.

The best thing Reagan could do to establish an anti-inflationary environment would be to open discussion of such a real gold link for the dollar. It would be one way of convincing long-term investors, who have abandoned the bond and other capital markets, to return to making long-term investments: the capital-investment boom without which the Reagan economic program cannot succeed.

Certain Reagan advisers are also known to favor linking the dollar to the European Monetary System as a way of drawing into closer collaboration with our continental European allies on stabilizing the gyrating foreign-exchange markets. While this would be difficult in the short term, German banking sources reported this week that such a "real gold price" of about $450 is realistic.

In fact, Hans Bresser, board member of the Dresdner Bank, hinted broadly at a Madrid conference this week that the Bundesbank, if not the EMS as a whole, is considering formally monetizing its gold, by mobilizing gold to defend the West German mark. Speculators against the mark, he said, "should not forget gold. The Bundesbank has 3,000 tons of gold in reserve, which are presently valued at 14 billion deutschemarks but which would be worth DM 95 billion [over $47 billion] valued at market prices of $500 per ounce. De facto, our total reserve would then be at DM 144 billion. With that sum, Germany can weather" the markets, he said.

"The Bundesbank would have no part in a package that would sell one ounce of gold," Dresdner told us, however. "That would be tantamount to a declaration of bankruptcy."

Rather, the Bundesbank is contemplating the use of the gold as collateral for loans from a large dollar holder. This could only be an OPEC nation such as Saudi Arabia, which, according to Chase Manhattan in New York, is "very interested" in puchasing gold-backed bonds.

If such gold-backed loans were done in quantity, it would be a firm step toward an entirely new gold-based international monetary system centered on the EMS.