IGWT Report

From Wedlock to Deadlock: The East-West Divorce

Brent Johnson debates Louis-Vincent Gave on de-dollarization.

- **We are in the process of a divorce between the global East and the global West as we move from a unipolar to a multipolar world. As with any divorce, major changes will be unavoidable. It is likely that everyone involved will be negatively impacted, at least in the shorter term.**
- **The US and China are both relatively self-sufficient with regard to their energy needs. The vital question will be what currency other countries will accept for their goods, particularly oil.**
- **Just because China and the global East are attempting to de-dollarize, this does not mean that it is guaranteed to happen. Many factors remain uncertain.**
- **The global East, in particular China, views de-dollarization as a political priority and are likely willing to endure economic harm in order to achieve this goal.**
- **China used to be highly dependent on US markets as a purchaser for their goods. This seems to be changing as emerging markets are becoming more important due to economic booms in many emerging countries including India, Türkiye, and Indonesia.**
- **Europe is turning out to be the neglected child in this divorce after grossly misplaying the geopolitical chess game in the last three years.**

This debate focuses on the highly topical issue of de-dollarization, featuring two of the most prominent voices in global finance today: Brent Johnson and Louis-Vincent Gave.

Brent Johnson has been vocal about his belief in the enduring strength of the US dollar. He argues that the US dollar will not only remain the world's reserve currency but also experience a significant spike in a "violent" global debt crisis. His *Dollar Milkshake Theory* posits that the US dollar will continue to draw strength from the global financial system, challenging the notion of de-dollarization.

On the other side, Louis-Vincent Gave, a renowned economist and financial strategist, offers a contrasting view. He opines that de-dollarization is not a mere possibility but a reality that the world is gradually moving towards. According to Louis, the global economic landscape is shifting, with nations increasingly exploring alternatives to the US dollar for international trade, potentially leading to a gradual decline in the US dollar's dominance.

This discussion is a riveting exploration of the future of global currencies, featuring insights from two of the most respected minds in the field, an intellectual clash that will enhance your understanding of global finance and the role of the US dollar in the world economy.

Louis-Vincent Gave is the CEO of Gavekal, a Hong Kong based company he co-founded over twenty years ago with his father Charles and Anatole Kaletsky. Gavekal has grown to become one of the world's leading independent research providers to institutional investors around the globe. Louis has written seven books, the latest being *Avoiding the Punch: Investing in Uncertain Times* with reviews how to build a portfolio at a time of rising geostrategic strife, and when very low interest rates and stretched valuations on most assets announce constrained returns on most assets over the next decade.

Brent Johnson brings twenty-five years of experience in the financial markets to his position as CEO of Santiago Capital. He has a long career in finance, having also been Managing Director at BakerAvenue, a USD 2bn Asset Manager and Wealth Management firm. Before joining BakerAvenue, Brent spent nine years at Credit Suisse in their private client group. Brent regularly gives interviews and speaks at conferences regarding precious metals, currencies & macroeconomic trends. His views have been quoted in numerous print, online and television outlets. He lives in San Juan, Puerto Rico with his wife Mary and son Moses.

This debate was recorded on April 30, 2024. **The video of the debate can be viewed on YouTube.**

The big question is whether the US dollar will retain its centrality or will it be supplanted within the next decade?

Ronnie Stöferle
Gentlemen, we will now dive into a discussion on topics ranging from de-dollarization, global macro trends, the status of the Japanese yen, and the developments in the world of gold and Bitcoin. These topics are like a complex 3D puzzle that we aim to piece together. Louis is particularly renowned for his analogies; he once compared the US dollar system to Microsoft Windows, noting how, despite its flaws and occasional malfunctions, it remains the dominant operating system, much like how the US dollar continues to lead among global currencies. This leads us to the overarching **question of whether the US dollar will retain its dominance, or will it be supplanted within the next decade**. Louis, could you share your perspective on this?

To replace it, you need not only a better system but a much better one that everyone changes to at once.

Louis Gave
First, let me start by saying the reason we're speaking English is that it's the easiest language to speak badly, relative to any other language, it's become the lingua franca of the world. Now, will the US dollar still be the dominant currency over the next 10 years? Yes, as I've said in my books, the US dollar is the Microsoft of the world. **To replace it, you need not only a better system but a much better one that everyone changes to at once.** Having said that, the story of the past 20 or 30 years, while Microsoft was still dominating and doing a great job, you actually did better with Apple, right? If you bought Microsoft in 2000, it was a 500bn market cap, and it's now over two trillion. But Apple was a 50bn market cap and is also over two trillion today. In the past 20 years, Apple created a new operating system. They invented the smartphone, and from there, a lot of people moved to a new operating system, which was Apple's operating system, sometimes running both side by side.

There's no reason trade between Mexico and China or South Africa and Zambia, for instance, needs to be priced in US dollars.

This is, in my view, what the RMB is trying to do. China has said the growth in the world over the next 20 years will be in trade in emerging markets. **There's no reason trade between Mexico and China or South Africa and Zambia needs to be priced in US dollars.** They are attempting to create a new operating system. And lo and behold, this is happening. We now live in a world where 20% of oil is no longer priced in US dollars. Just like it would have seemed absurd for Apple to be on 30% of operating screens around the world 20 years ago, this would have seemed like madness.

The only growth in trade in the world now is emerging market to emerging markets.

So you can chip away at it through specialized trade. **The only growth in trade in the world now is emerging market to emerging markets** for a number of reasons, whether it be geopolitical, such as the Russia sanctions, or financial, such as China offering great financing terms to Africa and Southeast Asia. So it is a changing world, and I think the Apple analogy to Microsoft works decently well.

The world is clearly going through a divorce. When you go through a divorce, some things have to change.

Brent Johnson
Yeah, I actually like that analogy. **The world is clearly going through a divorce. When you go through a divorce, some things have to change**, like buying a new house or changing insurance. I don't think the monetary system will look the same in 10 years, but I agree that the dollar will still be dominant.

A lot of people look at this divorce and automatically think they'll go with Apple because it's the cool new thing. But remember, Steve Jobs wasn't the nicest guy and got fired. Apple went through tough times. So **when discussing de-dollarization, people think it's a foregone conclusion and will happen quickly and peacefully.**

Any transition that puts another system on par with the dollar or replaces it will cause incredible economic volatility and possibly military violence.

But I believe **any transition that puts another system on par with the dollar or replaces it will cause incredible economic volatility and possibly military violence**. In that process, the dollar could go higher. I don't think Microsoft and Apple will develop and operate peacefully alongside each other in this scenario. Just because Apple is the cool thing in the real world doesn't mean Apple will be the cool thing in this scenario.

Niko Jilch[1]

Louis, could you expand on this and China's broader economic ambitions?

Louis, could you perhaps summarize your viewpoint on China's strategic plans, especially in terms of its monetary policies? You've articulated some compelling comparisons, including how Beijing manages its central bank akin to Germany's Bundesbank approach, which intrigues us Austrians and Germans. **Could you expand on this and China's broader economic ambitions?**

Louis Gave

Foreigners believe the US's greatest comparative advantage is the US dollar, which allows for funding budget and current account deficits without constraints.

I agree that any transition is unlikely to happen without military violence, as we've seen in Libya and Iraq. Americans believe their greatest comparative advantage is the rule of law, world-class universities, entrepreneurs, natural resources, and the inability to be invaded. However, **foreigners believe the US's greatest comparative advantage is the US dollar, which allows for funding budget and current account deficits without constraints**, as seen after the 2008 mortgage crisis.

Chinese policymakers recognize the US dollar's importance and question why they should fund US growth using the dollar.

Chinese policymakers recognize the US dollar's importance and question why they should fund US growth using the dollar. When Xi Jinping became president, his focus shifted from domestic issues to an "imperialist vision" of China's future. This vision includes initiatives like One Belt, One Road, the Silk Road Fund, and the Asia Infrastructure Investment Bank. It's not about invading neighboring countries but rather a "road building exercise" to facilitate trade and the flow of commodities and finished goods.

To move away from the dollar, the renminbi needs to be a strong currency, and the RMB bond market must be a reliable store of value.

Given this vision, China aims to de-dollarize emerging market trade to avoid paying tribute to its geopolitical rival, the US. **To achieve this, the renminbi needs to be a strong currency, and the RMB bond market must be a reliable store of value.** Currencies serve as a means of exchange, a unit of account, and a store of value, with bonds and equities as options for the latter.

Emerging market central banks must be convinced that RMB bonds will hold their value and keep reserves in renminbi. Over the past 10 years, China has followed a policy similar to Germany's in the 1970s, prioritizing the bond market and maintaining a steady currency.

---

[1] Over the past few years, Niko Jilch has contributed numerous articles to the *In Gold We Trust* report. He works as a financial journalist and podcaster. You can follow him on www.nikojilch.com, X, and YouTube, among others.

My concern with this arises when people assume that just because China is trying to achieve something, they will be successful.

Brent Johnson
I completely agree with Louis' characterization of what China is trying to do. I have no issue with his explanation. However, **my concern arises when people assume that just because China is trying to achieve something, they will be successful**.

I believe it will be much harder to accomplish in reality than to write about in a book. For instance, part of the reason China's bond market has remained relatively flat is due to their quasi-pegged currency and interest rates, which have been kept low because they had largely shut down their economy until recently.

I believe it will be much harder to accomplish in reality than to write about in a book.

There is no significant external holding of RMB bonds; it's mostly internal. Despite this, the Chinese yuan has lost 15% of its value in the last two years. So, when people say the rest of the world will stop holding US bonds because the dollar is losing value and start using the yuan instead, it's worth noting that even though the US dollar is supposedly losing value, the yuan has lost 15% against it.

The other reason Chinese bonds have outperformed US bonds is because the US purposefully increased rates, which causes bond prices to fall. Now, **I'm no fan of central bankers, but they definitely understand that raising rates leads to falling bond prices.** This idea that the US is shocked by the performance of treasuries is, in my opinion, off base. Of course, they knew raising rates would lead to lower bond prices.

The US has purposefully weaponized the dollar over the last couple of years.

I will argue until the day I die that **the US has purposefully weaponized the dollar over the last couple of years**. Higher interest rates and a blowing out of the budget are often used as evidence that the dollar can't last forever. However, considering the current state of the world, **higher rates in the US affect the rest of the world more than the US itself because the world uses dollars**. Although they're starting to use Apple as well, they still use Microsoft, and they owe a lot of money to Microsoft. In other words, the **world owes over 30 trillion in US dollar-denominated debt and another 80 trillion in off-balance sheet derivatives in US dollars.**

I don't see how we can transition from one system to another or even have dual systems without reconciling all that outstanding US dollar debt?

So, I don't see how we can transition from using Microsoft to Apple. If everyone starts using Apple, where will they get the money to finance, service, and pay off all the US dollar debt? In other words, the process of de-dollarization, if it takes place, pushes the US dollar higher, not lower. If there's less circulating, there's less supply, but all that historic US dollar debt still exists. **I can't figure out how we can transition from one system to another or even have dual systems without reconciling all that outstanding US dollar debt.** Until that gets reconciled with, I think we have the US dollar to contend with.

Is the 'dollar milkshake theory' actively in effect?

Ronnie Stöferle
Brent, considering the performance this year, where stocks, rates, the US dollar, and gold are all up, **would you assert that the 'dollar milkshake theory' is actively in effect?**

Brent Johnson

Yes, we've observed significant rises—8% in the dollar, 30-40% in gold, and 40-50% in equities, alongside increased rates.

Yes, this is evident this year. Reflecting since 2018-2019, when I initially discussed this concept, **we've observed significant rises – 8% in the US dollar, 30–40% in gold, and 40–50% in equities, alongside increased rates**. This clearly illustrates the 'dollar milkshake' effect, with the US outperforming globally.

The renminbi has fallen 15%, and the Chinese real estate market is down 60%. I question how China is winning in this situation.

While Louis rightly noted the trading increases between emerging markets, the majority of economic growth in the world continues to stem predominantly from the United States. Again, **I don't have a problem with China. The issue arises when people automatically assume China will win in this scenario**. Consider the last 10 years: the Chinese stock market is down 60% from its high, its down 30% from when Xi Jinping took over. **The renminbi has fallen 15%, and the real estate market is down 60%. I question how China is winning in this situation.** If these numbers applied to the United States, I'd receive countless messages about the empire's decline. Yet, because it's China, people believe it's a strategic move we don't understand. **Everyone should adopt a more neutral perspective.** After all, nobody knows how this will unfold. I often find myself in discussions or arguments with those who hold an absolute view that things can't be different.

Niko Jilch

What does "winning" in this context actually look like?

What does "winning" in this context actually look like?

Brent Johnson

For the US, maintaining the status quo as it is would be considered winning.

Well, that's a very good question. I think for the US, maintaining the status quo as it is would be considered winning. However, whether that's a true victory is debatable.

Louis Gave

I would say that providing better life outcomes for citizens should be the first goal.

I would say that providing better life outcomes for citizens should be the first goal. For instance, not having a falling life expectancy or a life expectancy at a 30-year low, which is the current situation in the US. It should be about reversing the rising infant mortality rate, not contributing to it. Winning could also mean not having 1.5% of the population in prisons and not having a Gini coefficient that increasingly resembles an emerging market.

People are concerned about the US struggling because they see issues firsthand, such as the homeless crisis in major cities, rising crime rates, and other social factors that indicate a sick society. The US today has the same life expectancy as it did 30 years ago, despite spending twice as much on healthcare as a percentage of GDP than 30 years ago.

The stock market's performance isn't even on Xi Jinping's list of priorities. Only 10-12% of Chinese people own stocks, mostly the rich

The reason I highlight this is, when Xi Jinping came to power 11 years ago, and Brent mentioned the stock market is down 30% since then, I don't think Xi Jinping cares. **The stock market's performance isn't even on his list of priorities**. Instead, he aimed to shift more of China's trade to RMB and reduce the economy's dependency on the dollar, which has been happening rapidly. This requires sacrifices, and if it means the stock market suffers, Xi Jinping doesn't care because **only 10-12% of Chinese people own stocks, mostly the rich**. It doesn't have the social impact we see in the West.

In China, most companies don't fund their growth through the stock market, so it's not as relevant to the leadership.

In China, most companies don't fund their growth through the stock market, so it's not as relevant to the leadership. They don't compare themselves to others based on stock market performance, unlike Donald Trump tweeting every time the Dow Jones is up 150 basis points. So it's a very different sort of perception of how you judge yourself. But this goes back, and I think this is really at the crux of this discussion, **what is a currency?** It's a **means of exchange, a unit of account, and most importantly, a store of value**.

US bonds are no longer a store of value; fortunately, US equities have been a terrific store of value. In China, it's been the opposite: bonds have been a great store of value, while equities have been a terrible store of value.

Historically, foreigners held US dollars as a store of value in one of two ways: bonds or equities. For a long time, both bonds and equities in the US were attractive options for storing value. However, for the first time in 30 years, we're looking at a five-year loss period in **US bonds, which are no longer a store of value**; **fortunately, US equities have been a terrific store of value**. **In China, it's been the opposite: bonds have been a great store of value, while equities have been a terrible store of value.** This might be due to China's strategy of convincing other governments and central banks to buy its currency, as they're more likely to buy bonds than equities.

If US equities stop being a store of value, as they do every 5-10 years, it's crucial that bonds become a store of value again.

If you're the US, you don't have to convince anyone to buy the dollar; it's already widely accepted. However, **if US equities stop being a store of value, as they do every 5–10 years, it's crucial that bonds become a store of value again**. Over the past few years, we've seen periods where people lose money on both equities and bonds, such as in 2022. If this continues for a year or two, it could raise a significant question about the US dollar as a store of value. **The US dollar used to be supported by two pillars: strong bonds and strong equities**. **With bonds no longer a strong pillar, the US dollar's position as a store of value is more precarious. If equities also falter, the US dollar's status could be in jeopardy.**

Ronnie Stöferle

Let's pivot our discussion to gold.

In our *In Gold We Trust* report, we have extensively discussed the decline of the traditional 60/40 portfolio model. Historically, this model thrived during an era coined as the Great Moderation, where inflation was not a significant concern. However, this dynamic has evidently shifted. Louis, you once made the point that the situation resembles the Chicago Bulls without Michael Jordan or the French national soccer team without Zinedine Zidane. This necessitates a fundamental rebuild of the portfolio structure. **Let's pivot our discussion to gold**, which may emerge as a vital diversifier in today's climate. Our new report is aptly named "The New Gold Playbook," reflecting the breakdown of conventional rules in the gold sector.

Do you think Xi Jinping cares about the price of gold?

You mentioned that Xi Jinping doesn't seem to care about the Shanghai Composite or Chinese equities. **Do you think he cares about the price of gold**? China, through the People's Bank of China, has been purchasing gold consistently, with 17 consecutive months of straight monthly purchases. Despite this, gold only accounts for about 4.3% of the People's Bank of China's total reserves, compared to a global average of 13%. Notably, the US holds approximately 70% of its reserves in gold, suggesting there is potential for the People's Bank of China to further increase its gold reserves. **An intriguing statement from a Chinese official was that China owns gold "through its people". Do you think gold plays a role**

for China, or is it perhaps overemphasized by the broader gold community?

Louis Gave

I don't think Xi Jinping cares about the gold price. For him, gold is a means to an end.

Look, I think to answer your question directly, **I don't think Xi Jinping cares about the gold price. I think gold for him is a means to an end**, as he's looking to reduce China's dependency on the US dollar and de-dollarize emerging market trade. Regarding China buying gold, it's important to note that gold demand is primarily driven by emerging markets.

When emerging markets do well, gold does well, and when they do badly, gold also suffers.

Gold is a play on emerging markets, where physical demand is concentrated in countries like China, which accounts for about a third of global gold demand, India with another third. People in emerging markets are the ones who predominantly buy physical gold. **When emerging markets do well, gold does well, and when they do badly, gold also suffers**. Although gold is often seen as inversely correlated with the US dollar, the past 18 months have shown that gold demand can remain strong even when the dollar is strong, as emerging markets continue to perform well. When the dollar's weak, emerging markets tend to do even better, but **you don't need the dollar to be weak anymore for emerging markets to do well**, which is a very important change we're going through.

You don't need the dollar to be weak anymore for emerging markets to do well.

Gold is a hedge option for the world falling apart due to wars, geopolitical reasons, financial crises, or other bad scenarios.

So that's the first function of gold. The second function, typically focused on by Westerners, is that **gold is a hedge option for the world falling apart due to wars, geopolitical reasons, financial crises, or other bad scenarios.** We've had a glimpse of this, and while China has been buying a lot of gold, **the big new marginal buyer has been Japan**. In March, after the BOJ announced it would sit on the yield curve forever, the yen moved from 146 to 155 very quickly. Japanese investors started buying gold like crazy, as evidenced by the increased volume in the main gold ETF in Japan, 1540JT, trading at a 10% premium to NAV.

This suggests that Japan cashed in on the second option, the hedge against financial repression or geopolitical crisis. This raises an interesting question because Japan's situation, with a collapsing yen and high debt, could potentially happen elsewhere. It's not a stretch to think it could happen in Europe, where France is running a 5.5% of GDP budget deficit at a time of full employment and economic recovery. The same could be said for the US, with full employment and budget deficits of 6% of GDP.

While a third of US debt is owned by foreigners, only 4% of Japanese debt is owned by foreigners.

While the stock of debt may not be as high in Europe and the US, the budget deficits will get them there over time. Additionally, the **ownership structure of the debt is very different, with a third of US debt owned by foreigners, 4% of Japanese debt is owned by foreigners**, while more than 40% of French debt is owned by foreigners. This means that in these countries, things can move much quicker.

For China, gold is a means to an end. It's a way to give credibility to their currency and to de-dollarize their trade.

Does the Chinese government care about the gold price? No, they don't. For them, **gold is a means to an end. It's a way to give credibility to their currency and to de-dollarize their trade**. They can tell other countries that they will trade in renminbi and if they don't want to keep the renminbi, they can trade at the

Shanghai gold market, offering gold in exchange for renminbi. This is particularly attractive for countries like Russia, Kazakhstan, and those in the Middle East.

China is the biggest gold buyer in the world and the biggest gold producer in the world.

China is able to do **this as the biggest gold buyer in the world**, importing about a third of global gold production each year. Additionally, it is **the biggest gold producer in the world**, which might explain why the central bank governor says they are okay on gold. They have a significant amount of gold in the ground, and if they ever need to get it out, they can simply put more resources into it. It's like how Canada doesn't have gold reserves in its central bank because if they need it, they can just go get it from their own land.

Brent Johnson

Winning in the global political and economic landscape means that the government stays in power.

Let's revisit the concept of 'winning' we discussed earlier**, winning in the global political and economic landscape means that the government stays in power**, whether it's the US government, the CCP in China, or Putin's party in Russia. While it's comforting to believe that our leaders prioritize the interests of their citizens, the reality is that their primary goal is to maintain their power and the power structure of their respective governments.

Gold is poised to benefit significantly from this geopolitical power struggle.

In this "game of thrones," every nation is looking to expand its influence and control over the global kingdom. As a result, **gold is poised to benefit significantly from this geopolitical power struggle**. The price of gold is likely to rise, as it has historically served as a hedge against economic and political uncertainties.

The US also confiscated its citizens' gold in the past, and they would absolutely do it again if necessary to maintain power.

When I hear someone from China, particularly from the CCP, say, "our citizens' gold is our gold," I'm reminded that the **US also confiscated its citizens' gold in the past**, **and they would absolutely do it again if necessary to maintain power**. The same would apply to China, Russia, or any other country facing such a situation.

The primary motivation for individuals in Asia buying gold is to protect their daily living expenses from currency devaluation.

The recent surge in gold demand in Asia, particularly in Japan, is not solely driven by concerns about the US dollar. In fact, when people in Asia buy gold, it's often because their own currencies, like the yuan or the yen, are losing value. While the dollar may be a secondary concern**, the primary motivation for individuals buying gold is to protect their daily living expenses from currency devaluation.**

Central banks want to diversify their reserves, especially after witnessing the US freeze Russian assets.

Central banks also have their reasons for acquiring gold. **They understand that fiat currencies eventually lose value over time**, and even if they don't completely collapse, they still lose purchasing power. Since their currencies are not the US dollar, they need an alternative form of currency to conduct international transactions. **They also want to diversify their reserves, especially after witnessing the US freeze Russian assets.** This has led many countries to seek alternatives to the current global financial system, with gold being a prominent option.

Gold is not a "silver bullet" that can solve all economic problems. Gold's value and demand are influenced by various factors.

Gold is undoubtedly a crucial component of any investment portfolio, as it has historically served as a hedge against economic and political uncertainties. However, **it is not a "silver bullet", pardon the pun, that can solve all economic problems. Gold's value and demand are influenced by various factors, including local currency strength and central banks' desire to diversify their reserves.** Therefore, while gold is an essential part of a diversified portfolio, it should not be viewed as an all-encompassing solution to the complex challenges of international politics and finance.

Until a new system incorporating gold is in place, using gold will remain less efficient.

Gold isn't the most convenient asset to move around the world. It can be done, but **is China really going to import all this gold just to start shipping it abroad to settle its trade balance?** Gold has been used for centuries, and it can still be used, but it's not as efficient, easy, or quick as the current system. **Until a new system incorporating gold is in place, using gold will remain less efficient**. Some countries might still use it to de-dollarize, despite the inefficiency. However, it's worth noting that **attempts to use gold by smaller countries in recent years have often failed.** So while gold is an important asset and everyone should own some, it's not a silver bullet that solves all economic problems.

Louis Gave

China wants to create their own international gold exchange in Shanghai, but that would imply that all the other nations place their trust in China.

The initial Bretton Woods days saw countries like France, the UK, and Germany storing their gold in New York, facilitating trade settlements by simply moving gold bars between designated boxes. However, the loss of faith in global institutions and the US, particularly after the Russian sanctions, has led to a shift in gold usage. China won't store its gold in New York; they want to create their own set of gold boxes in Shanghai, but that would imply that all the other nations place their trust in China.

China is creating dependency similar to the US post-World War II.

China's Belt and Road initiative, which involves building infrastructure in other countries and establishing long-term financial dependencies, could potentially create a new dynamic where gold is used for trade settlements. By building high-speed rail lines and nuclear power plants in countries like Indonesia, **China is creating a level of dependency similar to the US post-World War II**.

Russia and Kazakhstan, which are more dependent on China, may have less choice in trusting China to hold their gold.

Countries like **Russia and Kazakhstan, which are more dependent on China, may have less choice in trusting China to hold their gold**. However, the extent to which other countries will follow suit remains an open question. The reality is that the shift towards using gold in trade settlements is slowly building up, with more and more trade being settled in this manner.

Niko Jilch

Within this framework, **who does one trust?** The CCP, the state, or Xi Jinping himself?

Louis Gave

Trusting China means trusting the Chinese Communist Party.

In China, the party and the state are intertwined, with the party constitutionally positioned above the state. **Trusting China, therefore, means trusting the Chinese Communist Party**. While one might speculate about political evolution, the party's ideology currently views such changes as an impossibility.

Are we seeing "de-euroization"?

Ronnie Stöferle
Talking about divorce and its complexities, in this ménage à trois, Europe is often overlooked amidst the dominant narratives of the US and China. **Are we seeing "de-euroization"?**

Yes. The world is going through a divorce. This reflects a broader geopolitical trend where alliances are shifting, and cooperation between major powers is becoming less certain.

Brent Johnson
In my opinion, yes. And for a couple of very specific reasons. **This world is going through a divorce**, as I mentioned earlier. It seems to be a mutually desired divorce, with both the US and China seeking to decouple from each other to a significant extent, while acknowledging that some level of business interaction will persist. This shift is not solely driven by the East or the West. Rather**, it reflects a broader geopolitical trend where alliances are shifting, and cooperation between major powers is becoming less certain.**

China's distancing from the West is hurting Europe adversely and the US appears to be prioritizing its interests over its alliance with Europe.

China is taking steps to insulate itself from the West, though not entirely severing ties. Previously, China relied heavily on imports from Europe. Contrary to some expectations, Europe's alignment has not leaned towards Russia or China against the US. **China's distancing from the West is hurting Europe adversely.** Concurrently, the **US appears to be prioritizing its interests over its traditional alliance with Europe**. This strategic realignment is observable in the significant outflow of industry from Germany, some relocating to China and others to the United States. At a recent entrepreneurial conference in Germany, attendees noted a trend of talented individuals migrating to other European countries such as Liechtenstein and Switzerland, as well as destinations outside Europe like Dubai. This shift underscores Europe's position as the disadvantaged party in this geopolitical recalibration, a situation unlikely to change soon.

Europe is like the child who is left disadvantaged after the divorce.

Ronnie Stöferle
Europe is like the child who is left disadvantaged after the divorce. A friend of mine in the automotive sector emphasized the increasing presence of Chinese cars in our markets in the coming years. This trend poses a significant challenge to German automakers such as BMW, Mercedes, and Porsche, which have historically taken pride in their industry. I agree that Europe is emerging as the primary casualty of this geopolitical transformation.

Europe had a significant opportunity to act as a mediator in this geopolitical separation. However, due to policy failure, it failed to do so.

Louis Gave
As a European who left Europe, the type Brent described, allow me to interject. **Europe had a significant opportunity to act as a mediator in this geopolitical separation. However, due to policy failure, it failed to do so.** There is a quote from Tolkien's "The Lord of the Rings" that resonates with me: "One ring will always corrupt, two will divide, but with three, there is balance." This notion, applied metaphorically, speaks to the potential for a balanced global order with the US, Europe, and China each wielding influence.

China's emergence as a major exporter of automobiles, heavy machinery, and agricultural equipment has reshaped the competitive landscape.

However, Europe faltered in fulfilling this role. Consequently, we find ourselves in a "two ring" world, as Brent suggested. Notably, **China had become an industrial powerhouse and transformed global trade dynamics. Its emergence as a major exporter of automobiles, heavy machinery, and agricultural equipment has reshaped the competitive landscape.** The remarkable productivity gains in Chinese industries have propelled its status as a leader in global manufacturing. **This shift has created a self-reinforcing**

industrial ecosystem, providing China with a substantial competitive advantage that will be difficult for other nations to match.

The yen valued at 160 or higher will kill the competitiveness of European industries.

This makes it very hard for other countries to compete or to catch up. Europe, in particular, faces a dual threat: the depreciation of the yen and intensifying competition from China. **A yen valued at 160 or higher will kill the competitiveness of European industries**, including Germany, Sweden, Switzerland, and France. This unfavorable exchange rate, coupled with China's industrial might, presents a one-two punch for European businesses.

Now, **let's not kid ourselves that the US won't face the same punch**. The latest GDP numbers show a core CPI inflation rate of 3.7%, while GDP growth is only 1.6% This is not a sign of a healthy economy; it's an economy where inflation is twice the growth rate of real GDP. Additionally**, the US is expensive**. Traveling in the US, everything feels overpriced compared to other parts of the world. In the past, the US felt super cheap outside of expensive pockets like New York and San Francisco, but this is no longer the case.

Asia has a significant comparative advantage in terms of industry productivity and cost of goods.

Japan, on the other hand, is surprisingly affordable; you can't spend money even if you try. Europe is somewhere in between, not super cheap, not super expensive. The US is super expensive, while **Asia has a significant comparative advantage in terms of industry productivity and cost of goods**. The gap is too big.

Brent Johnson

In a global divorce, all major economies, including the US, China, Europe, Japan, and others, will face difficulties.

Louis's perspective on the global economic situation has made me realize that it's essential to acknowledge that **all major economies, including the US, China, Europe, Japan, and others, will face difficulties** and "take a hit". Despite the potential for the US to experience significant impacts, it's not a given that it will lose its global hegemony as a result. Bullies, like the US, often maintain their position due to the reluctance of others to confront them.

Outside of the US, markets may not be large enough for China to sell all their production at current prices.

However, I agree that eventually, bullies can fall, but the process might not be immediate. For de-dollarization to occur on a large scale, China would need to decouple from the US, which would be a challenging process. **While acknowledging the significant productive capacity and economic strength of China** and other countries, it's also important to consider that **outside of the US, markets may not be large enough to sell all their production at current prices.**

If China has to start selling to new markets at lower prices, it may not be able to service and pay off its debt effectively.

Both the US and China have accumulated considerable debt over the past 20 years, China's debt levels increasing significantly. **If China has to start selling to new markets at lower prices, it may not be able to service and pay off its debt effectively**. Russia is an outlier in this scenario, as it hasn't taken on much debt and possesses substantial natural resources, which has helped it weather sanctions and other pressures. As the world continues to decouple along East-West lines, **I don't think China can maintain its position as well as Russia has.**

Louis Gave

The first big question is who's on the other side of the debt - is it domestic or foreign?

I think on debt, for me I look at debt a little bit differently. **The first big question is who's on the other side of the debt – is it domestic or foreign?** For example, if I borrow a million dollars from my dad, as a family, we don't have any debt. But if I borrow a million dollars from Brent, I owe Brent a million dollars. When it comes to the growth of debt in the US and Europe, in countries like France, it's increasingly owed to foreigners. This narrows policy choices compared to when debt is owed domestically. When you owe it to yourself, you can kick the can down the road for a very long time, as Japan has shown.

The other question is what is done with the debt. What did the US get for it's USD 34trn of debt?

The other question is what is done with the debt. When I started in this business, the US government debt was USD 4.5trn. Today, it's at USD 34trn. **I always ask myself, what did the US get for that USD 30trn?** Where are the major infrastructure projects like the Hoover Dam or the interstate highway system? A lot of that debt has gone to fund unproductive foreign wars and social transfer payments.

Once you give employment benefits, you can never take them back, while infrastructure projects have a definite end.

In 2008, I had a meeting with the then Hong Kong financial secretary. It was the darkest day of the darkest hours of the 2008 global financial crises. I asked him about Hong Kong's approach to the financial crisis, given its capitalist nature. Hong Kong, being very capitalist, had no welfare state or unemployment benefits. At the time, Hong Kong was running a big budget surplus. I asked if they were going to start paying unemployment benefits, and he nearly fell off his chair. He replied that they would pave the entire Victoria Harbor and build more bridges across the harbor before implementing unemployment benefits. **Once you give benefits, you can never take them back. Infrastructure projects have a definite end.**

Although there was a big increase in Chinese debt, the results were tangible in the form of visible infrastructure development.

He said they would do exactly the same across the border in China, and sure enough, China responded to the 2008 crisis with an all-out infrastructure spending plan. **Although there was a big increase in debt, the results were tangible in the form of visible infrastructure development**. They've built high-speed rails, roads, ports, and airports. While the productivity of such infrastructure can be debated, it's generally more productive than, say, funding a hip replacement for a grandmother.

Economic activity is energy transformed. Most countries save US dollars to buy energy, especially oil.

When comparing debt, are we really talking about the same thing? I'm not 100% sure that we are. Here's a critical point: **economic activity is energy transformed. Most countries save US dollars to buy energy, especially oil**. In the past, dollars were saved to buy Caterpillar machines and Ford trucks, but that's no longer the case. Today, no one wants a Ford truck. If you want a Caterpillar, you'll probably buy a LiuGong machine because it's cheaper and just as good, if not better. For many industrial goods, you no longer need dollars, but you still need dollars for energy and commodities.

The US became an energy superpower thanks to the shale revolution.

This brings me to the most significant macro development of the past 15 years that everyone seems to forget: **the US became an energy superpower thanks to the shale revolution**. The US added a Saudi Arabia in just 15 years. This, to me, is what has underpinned the dollar's strength and the US bull market.

If the US remains at the center of the next energy revolution and continues to have the cheapest cost of energy, the dollar will stay king.

The fact that the US had a much cheaper cost of energy and more plentiful energy than anyone else for 15 years has been a significant factor in the dollar's strength. The question now is, what happens over the next 10 or 15 years? **If the US remains at the center of the next energy revolution and continues to have the cheapest cost of energy, the dollar will stay king.** However, **China is making leaps and bounds in nuclear energy**, particularly in molten salt reactors, which I think are the energy of the future. China is also the leading provider in solar energy, by a long shot. If you believe in wind energy, then Germany and Scandinavia could have a shot at being energy leaders.

If you think that in 10 years time, the US will still be the main driver of the marginal increase in energy in the world, then the US will stay king. However, this is not my belief, as the US has stopped investing in this field for the past seven or eight years.

The game of nominal value of money is over as this system does not allow to control the supply of resources, our product, our rules. We don't play by the rules we didn't create."
Alexei Miller, CEO of Gazprom

Ronnie Stöferle

Louis, energy is a great point, quoting Alexei Miller, the CEO of Gazprom, who stated, "**The game of nominal value of money is over as this system does not allow to control the supply of resources, our product, our rules. We don't play by the rules we didn't create."** In this *In Gold We Trust* report, we write about the gold drain that the United States experienced. Many decades ago, the US had approximately 30,000 tons of gold, but countries running current account surpluses like Germany and France were building up their gold reserves. The gold drain became increasingly significant, and on August 15, 1971, they stopped it, "temporarily" ending the peg of the US dollar to gold. This reminded me of something Peter Miller once told me, which led me to the OPEC library in Vienna.

Do you think that at some point, organizations like BRICS or the Shanghai Cooperation Organization will decide to sell their resources in currencies other than the dollar?

I found a document stating that, on October 7, 1971, OPEC announced that due to the new situation in the United States, noting that these developments have resulted in a de facto devaluation of the US dollar, the currency in which posted prices are established vis-a-vis the currencies of the major industrialized countries. **They mentioned that OPEC member countries shall take necessary action, such as establishing negotiations individually or in groups with oil companies, to offset any adverse effects on their per barrel real income** resulting from international monetary developments as of August 15, 1971. I found this quite fascinating, as it's not something you read about often. The question then arises: considering the shale revolution and the fact that Europe is weaker than emerging markets and the United States in terms of energy and resources, **do you think that at some point, organizations like BRICS or the Shanghai Cooperation Organization will decide to sell their resources in currencies other than the dollar?** We've already seen some shifts in this direction, but it hasn't yet become a major topic. So, what's your view on that?

Russia, being one of the top three oil producers in the world, has now moved away from the US dollar. The question remains whether the Middle East will follow suit.

Louis Gave

We've transitioned from 0% to 20% of oil being priced in currencies other than the US dollar. **Russia, being one of the top three oil producers in the world, has now moved away from the US dollar. The question remains whether the Middle East will follow suit.** In the near term, looking at the next few years, it's unlikely due to their dependence on US protection, with the exception of Iran, of course. Iran has also moved completely to non-US dollar sales, selling its oil to China in RMB. China's first goal was to obtain all its imported oil in its own currency rather than US dollars, and they're more than two-thirds of the way there now with Iran and Russia accepting 100% RMB for both oil and natural gas. They've also signed natural gas contracts with Qatar for RMB. China has made significant progress towards their goal, as they're about two-thirds of the way on natural gas as well. This change is already important for them, as it allows them to pay for their oil in their own currency.

Once you've moved away from the US dollar, you've eliminated the most significant restriction on your growth China is already about two-thirds of the way there.

Once you've moved away from the US dollar, you've eliminated the most significant restriction on your growth, right? You can always print more of your currency and avoid international sanctions. China is about two-thirds of the way there, but convincing Saudi Arabia to follow suit may be too much of a challenge. Instead, China is focusing on ensuring that the two-thirds they have is sufficient. That's why they're investing in nuclear, solar, and electric vehicles. By doing so, they aim to make the two-thirds of their energy needs they can obtain through these sources enough for their requirements. There's a higher chance of this happening through nuclear, solar, and investments in pipelines to Russia and Kazakhstan than by convincing Saudi Arabia to change its currency preference.

The shale revolution made the US the largest energy producer in the world. This means we're not buying as much oil from overseas, and as a result, we're not sending as many dollars out into the world.

Brent Johnson

My take on this is that the oil-for-dollars deal, which happened after the embargo in 1973, not only established the oil-for-dollars regime but also led to the exponential growth of the Eurodollar market. This growth occurred over the past 40 years when dollars were plentiful due to the United States buying oil from overseas by sending dollars out into the world. Fast forward to 10–15 years ago, **the shale revolution made the US the largest energy producer in the world. This means we're not buying as much oil from overseas, and as a result, we're not sending as many dollars out into the world.** Despite this, the Eurodollar market has grown to USD 30trn, with USD 80trn in derivatives and swaps. The Eurodollar market faces challenges as the US no longer exports as many US dollars due to the shale revolution. This situation is further complicated by increasing global divisions and national divorce. Where do the other countries get the dollars to buy the oil?

The US isn't exporting dollars to the same extent as before.

While there has been discussion about 20% of oil trade being priced in currencies other than the dollar, the accuracy of this number is questioned. It could be that the calculation may include trade invoiced in currencies pegged to the US dollar or not taking place in US dollar. But I don't believe that 20% number is accurate. However, even if the 20% figure is accurate, it still poses a problem because **the US is not exporting dollars to the same extent as before.**

China's primary concern is facilitating transactions using renminbi. When you kick out Russia, it has consequences.

Louis Gave
The calculation is simple: you exclude Russia, and China has already engaged in renminbi transactions with countries like Kazakhstan and Qatar. Regarding the invoicing in renminbi, the distinction lies in the settlement. While they may not be priced in renminbi, they are settled in renminbi. **China's primary concern is facilitating transactions using renminbi.** You throw in the fact that Russia is a significant exporter of commodities, often ranking as the top or second in the world. **When you consider kicking out Russia, it has had consequences.** You move from 5% of the market not being priced in dollars to 20%.

The US is sending dollars abroad to service existing debt and purchase the commodities they need.

Talking about the US not exporting dollars, in 2023 the US current account deficit reached a record USD 880bn. This means the US is sending dollars abroad to service existing debt and purchase the commodities we need. So, the US is exporting dollars, it's never exported this much before.

Brent Johnson
That is true, but not for oil, and we agree that energy prices are rising.

After the shale gas boom, everyone expected the US current account deficit to improve, and it did from 2012 to 2017.

Louis Gave
The last time the US current account deficit was below USD 500bn was in 2006–2008, when the oil price was high. Since then, the US has had a shale boom, nearly eliminating its energy deficit. **Everyone expected the US current account deficit to improve, and it did from 2012 to 2017**. The US was exporting fewer dollars during that period.

But since 2020, the US current account deficit has exploded due to increased fiscal deficits of over 10% of GDP.

However, since 2017, and especially **since 2020, the US current account deficit has exploded** due to increased fiscal deficits. The US is now running twin deficits of over 10% of GDP. Typically, when a country reaches twin deficits of over 5% of GDP, the IMF gets involved. The US being the US, they can withstand 10% for a longer time, but let's not pretend that the US is not exporting dollars; it's exporting them like crazy. **For now, this hasn't been a major issue for the dollar, as US equity markets have been a dominant destination for investments.**

If the US stock market stops being a reliable store of value, it could potentially release more dollars into the global system.

The US equity market has been a significant store of value, with seven stocks driving much of the market's performance. However, **if the US stock market stops being a reliable store of value, perhaps due to a decline, it could potentially release more dollars into the global system**.

I don't think the US can have a recession without the rest of the world feeling it.

Brent Johnson
If you believe this divorce will not accelerate and instead lead to more cooperation, you're right. However, if you're like me and think the divorce will accelerate with more trade barriers and sides being chosen, I don't believe China will be able to sell all of their production at the current price. They may sell at a lower price in markets dependent on the United States. **I don't think the US can have a recession without the rest of the world feeling it.** That's where we may disagree. The countries you mentioned sell into the US, and the whole world is connected. You can't simply say they don't use the US anymore.

Most Westerners believe that if China can't export as much to the US, it's in trouble. However, China is the largest car exporter globally, yet we don't see these cars on US streets? The answer is zero.

Louis Gave

I believe the main difference in our views lies here. **Most Westerners believe that if China can't export as much to the US, it's in trouble. However, China is the largest car exporter globally, yet we don't see these cars on US streets? The answer is zero.** These cars are sold to countries like Indonesia, Saudi Arabia, and Chile. The trains, turbines, solar panels, nuclear and thermal power plants that China sells are not being sold in the US . They are increasingly sold across emerging markets. The growth in trade is happening primarily between emerging markets, particularly between China and emerging markets. As a result, China's dependency on the US decreases every year.

A decade ago, China was significantly dependent on the US, but this is no longer the case.

A decade ago, China was significantly dependent on the US, but this is no longer the case. TikTok serves as a perfect example. When the US demanded that China sell TikTok, they responded by saying it's only 17% of their business and they would rather shut it down than comply. This shows that China is willing to face consequences in the US to maintain their stance.

The view that China would be in trouble without the US is a US-centric perspective that may have been true 10 years ago, but no longer reflects the reality of China's trade flows today.

Could Europe have resisted siding with the West? And secondly, could Bitcoin emerge as a neutral trade currency in the next decade?

Niko Jilch

I'll combine two questions, concerning the euro and Bitcoin. Europe's attempts to de-dollarize via the euro, notably with a gas deal prior to the Ukraine conflict, aimed to diversify currency usage. However, geopolitical tensions led to a shift away from the euro. **Could Europe have resisted siding with the West? And secondly, could Bitcoin emerge as a neutral trade currency in the next decade?**

Without a significant geopolitical crisis, Europe aligning with China or Russia over the US is improbable.

Brent Johnson

Europe, historically, has been subservient to the US. **Without a significant geopolitical crisis, aligning with China or Russia over the US is improbable.** Another thing, when people say Russia no longer sells energy in US dollars and euros, only in rubles, it's a shell game. **Russia still gets US dollars and euros for their energy, but they've added a step in between**. They're not selling in anything other than rubles or yuan. As for a peaceful solution to this, I'd be happy to be wrong. But I feel like the dice have been rolled, and the leadership of these countries won't back down. They're all psychopaths who will do what they think they need to do to stay in power, causing more chaos and volatility.

Europe's loss isn't as much the US's gain as it is emerging markets' gain.

Louis Gave

Just before the Ukraine war broke out, **I thought this was Europe's big moment.** All of a sudden, Europe could get energy priced in euros. This was a bullish case for Europe, as **they would have access to cheap Russian natural gas in their own currency.** This would create a self-reinforcing cycle where Russia would buy European goods with the euros it earned. However, the war has thrown this opportunity out the window. **Europe's loss isn't as much the US's gain as it is emerging markets' gain.**

Russia has started selling energy in currencies like the Indian rupee and the Chinese renminbi, offering discounts to countries like India. This is a game changer for India and China, but it raises the question of what Russia can do with the rupees it earns. The renminbi is more useful to Russia, as they can buy products like cars, smartphones, and computers.

Regarding Bitcoin, it seems that countries like China and India prefer to pay in their own currencies.

This leads to the question of whether some of this trade could be settled in Bitcoin. Two years into the war, it's surprising that this hasn't happened yet. Initially, rich Russians moved their money into Bitcoin to avoid assets being frozen. However, two years later**, it seems that countries like China and India prefer to pay in their own currencies**. Russia is now selling commodities at a discount to countries like India, Indonesia, Korea, and China.

A significant economic boom that many people are overlooking is happening in countries like Türkiye, Mexico, and India.

A significant boom that many people are overlooking is happening in countries like Türkiye, Mexico, and India, which have outperformed the US stock market so far in the 2020s when considering US dollar terms. Emerging market debt markets, including countries like Indonesia, China, Brazil, and Mexico, have also significantly outperformed US debt markets by substantial margins. Despite challenges like Fed tightening, an emerging market crisis, and geopolitical tensions, this outperformance signals the start of a new emerging market cycle. This bull market has the potential to continue, especially since it's largely going unnoticed by the broader investment community.

Ronald-Peter Stöferle
Gentlemen, I thank you for this very inspiring debate!

The video of this debate can be viewed *here* and the *In Gold We Trust* report 2024 is available for download *here*.