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Swiss sound money advocate Claudio Grass talks to Professor Hülsmann about the consequences of extreme money production, an unhinged world and his role at Edelweiss Holdings.

Steering the ship in a rocky sea: A conversation with Guido Hülsmann

It's been a decade since you published *The Ethics of Money Production*, and we have since witnessed extreme and unprecedented monetary policies around the world. What are your observations regarding the economic and ethical consequences of these policies and how do they affect us all?

That's a large question, so allow me to give a short answer. Present-day monetary policies do not only distort the *general level* of the return on capital, but also the return *structure*. Savings are therefore discouraged, and the few genuine savings that exist are directed into uses where they will not bring fruit, while they are lacking elsewhere. Debt and leverage are everywhere, and step by step they are even creeping into former family businesses. Not only the financial world, but the entire economy has been turned into a house of cards, in need of constant assistance from central banks. The overall result is an "inflation culture" of epic proportions. Irresponsibility and indifference are rampant, along with an artificial concentration and firm sizes, materialism, haste, and various other effects.

Now, some of this is new as compared to what we saw fifteen or twenty-five or a hundred years ago. But in historical retrospect I see more continuity than novelty. Current monetary policies certainly are "extreme" and also "unprecedented" as far as banking *techniques* and the quantitative dimensions are concerned. But they pursue the very same *objectives* and also produce the very same *type of results* as previous generations of banks and central banks in the past 150 years, most notably, uninterrupted credit growth and bail-outs that undermine the very heart of the market economy. Clearly, we have no reason to relax our efforts, but neither should we expect the end of the world for tomorrow.

As a result, the pressure on individual and family savings has exponentially increased. How would you evaluate the state's role in the savers' struggle and what are the bigger-picture consequences of this trend, apart from its deleterious impact on social cohesion?

Virtually all of the pressure has come indeed from the state and our monetary authorities. Zero and negative interest-rate policies have discouraged savings directly, and the ever-growing debt facilities have destroyed the incentives to cultivate the virtues of frugality and financial self-reliance. As a consequence, there are ever-growing wealth disparities, all over the world. I think this is what you have in mind when referring to diminishing social cohesion. We also observe a massive return of what in former times has been called a proletarian mind-set. People who do not master their lives financially, and who have no hope of ever getting there, tend to expect others to take care of their various needs and to run after those who promise the most. The bottom line is an astonishing and very materialistic selfishness. This also tends to show up on the opposite side of the income and wealth spectrum. The well-to-do are often "all in" in their pursuit of ever more wealth.

What are your thoughts on what might lie ahead?

When you have to steer a ship in a rocky sea, you watch the sky for orientation, and also for comfort. Besides all the current known unknowns and all the unknown unknowns, there are a few principles and regularities on which we may rely. We know that the current policies are destructive. We know that unless this destruction is compensated by other factors it will lead to ever greater social and political conflicts. We should expect that such conflicts may tempt political leaders to seek short-run solutions involving even more financial repression on the one hand, and even more frivolous irresponsibility on the other hand. We know that such policies come at the short-run expense of savers, and at the long-run expense of nearly everyone else. We know that our responsibility is to preserve our capital as well as we can. We know that we have a reasonable chance to achieve our objective by owning participations in businesses that, like ourselves, prepare for a future beyond the troubled waters that lie ahead. We know that all other approaches boil down to gambling. We know that we do not like to gamble with our capital and, indeed, we never will.

If money can no longer be counted on to be a standard of measure, and if the calculation with respect to value is being frustrated so much, what options do we have with respect to deploying irreplaceable savings?

That's an important question and we have given much thought to it in the aftermath of the 2008 crisis and the post-crisis turn of economic and monetary policies. The bottom line is that in a monetary economy you cannot avoid using monetary figures, but today you have to use them with great circumspection and balance. We never prefer one investment over another merely in light of any financial results. The latter must be acceptable, but there are even more important criteria that also need to be met, such as the quality of people running the company, the nature of its results and the robustness of its operations. This is why we spend so much time assessing these criteria.

The popularity of hedge funds and others who have sought to pursue 'macroeconomic' strategies in money management seems to have waned. Most of these folks have failed. What do you see here?

I do not agree that all such approaches have failed. Many great fortunes have been built in the investment world by those who understood better, or earlier, than others the great tides separating bear markets and bull markets. At Edelweiss, too, we are positioned in such a way that the relative prices of our holdings would greatly increase if it ever came to a market meltdown. But it's true that we do not pursue a "macro strategy" or however you would call it. It's also true that most people who pursue such strategies fail. The reason is threefold. One, macroeconomic phenomena are very complex because of the high level of aggregation. Two, even if you knew the overall picture, you still have to make a call on concrete investments that somehow reflect the overall tendency that you expect. Three, price-level tendencies, interest rates, and stock-market movements very strongly depend on the actions of central banks. Hence, you need to guess correctly how far central banks will go to reach their objectives. What level of costs, in social, financial, political, and cultural terms, will they be willing to accept to reach their objectives? How would *you* know in advance? Each of these problems is quite formidable. Together they virtually guarantee that macro approaches fail most of the time.

In the current economic and investing environment, do you see a necessity to go back to basics as to what is a store of wealth and can you explain the real factors that contribute to it?

This is another difficult question. Let me again try to be very brief. I think you are referring to the significance of sound money as a foundation of all economic and social relations. As you know, I am fully convinced of its primordial importance. A sound money, such as the silver or gold coins in former times, gives the saver the reasonable option to save in cash. They do not have to invest savings to preserve them for tomorrow. This encourages savings, makes savings more independent and robust, and raises the bar for investments of all sorts, be it in industry, finance, or real estate. Now the monetary and banking reforms of the past two hundred years have destroyed that type of money. The dams broke after World War Two. Since then, monetary authorities pursued a policy of permanent price-inflation, pretty much all over the world. In such a world, it is suicidal to save in cash. As a consequence, savings have been discouraged and what remains of them is increasingly fragile, because they are concentrated in ever-fewer hands, which infers a sociological fragility, and, further, they are leveraged, which is financial fragility. Today we have reached the point where many people, despite the short-run incentives that are stacked against them, have returned to hold a significant part of their savings in precious metals. Many market participants have also made a return to gold holdings for monetary purposes. Gold is not anybody's debt and thus promises liquidity when you need it most. This is why central banks are currently stocking up their gold reserves. At Edelweiss Holdings, too, we believe this to be a sensible approach.

Professor Hülsmann, we both know each other from the Mises Institute and you are well known as a scholar. Most people however are unaware of your long-time role as an adviser to Edelweiss Holdings and now as Acting Chairman of its board of directors. I am personally familiar with the work that Tony and his team are doing with respect to capital preservation, but I'd like to know what have you learned about the practical and action-oriented aspects of this work.

My involvement with Edelweiss Holdings has indeed been a rich source of experience. As an independent director, you do not run the company. You are not an employee, but responsible only to the shareholders. Your mission is to make sure that the company is run in their long-run interests. This requires that you become sufficiently familiar with all the material aspects of current operations. Virtually all of this lay outside the field of my academic expertise. I had to give much thought and learn a lot about legal constraints and options, about the investment process, about our counterparties, legal and tax issues, shareholder issues, about internal operations, remuneration policies, board dynamics, and so on. Well, I am still a learner and probably always will be. I'm blessed to have very competent fellow board members on my side who fill in my many dark spots, a seasoned businessman such as John Brunner, lawyers such as John Hemingway, James Keyes, and Roderick Forrest, and then of course Tony Deden who knows everything about and around this work. I'm especially happy to have John Hemingway as a role model for what an independent director can and should be.

Tell me a bit about the practical discussions that take place within the investment team and what sets their approach apart from similar practices?

Look, our aim is to preserve and grow our capital in an increasingly unhinged world. We have no objectives relating to returns or time horizon. We do not spend any time whatsoever trying to develop quantitative models to guide or explain our investments. All our discussion pertains to what is often called "fundamental" analysis but in our case also involves a heavy dosage of subjective assessment as to risk and as to value. We assess the robustness of our information and weigh it in our own way. Sometimes this entails the necessity to think about rather philosophical subjects, such as the meaning of measuring, pricing, and valuing. How reliable are metrics in terms of money that can be changed from one day to another by the whim of a central-bank board? And then we discuss the merits of one investment compared to suitable alternatives, which might be other investments or no investment at all. We believe that this *process* of coming to our decisions, at the heart of which is plain critical thinking, constant revision of information, and open discussion across all levels of hierarchy, is, in the long run, more important than the decisions themselves. Coming from academia, I don't know quite how unique this approach is in the investment world. What I can say is that it seems to be very wise. And it also seems to me that it's more important to be right than to be original.

What would you say is your most important takeaway after coming face to face with the Edelweiss investment practice?

The most important takeaway is that in our company words and actions coincide. We do not have a sales department to attract customers by saying A, and then an investment team practising B. In fact, we have no sales department at all. Tony Deden often stresses that we are not in the business of attracting shareholders. That's correct, and it's that simple thing, which we might call moral and intellectual independence, that makes our work so different from the myriad of financial service-providers that you find elsewhere. It informs our objectives. It informs all the means that we deploy and all the means that we do not deploy. I think I did not quite realise the importance of this point when I became involved with Edelweiss. It's something that you need to experience. It's not something that can be fully grasped by reading shareholder letters, or which could be communicated in a classroom. But it truly is the root of our coherence and robustness.

Would you say that the moral and intellectual independence that you described also contributes to Edelweiss's results?

That's entirely right indeed. Without that independence, you cannot afford, or cannot suffer, to commit your resources to the long run. You will therefore be unable to reap the fruits that only come from long-term engagements. The financial firms of our day tend to be completely absorbed by the present, meaning the next few months or years. The reason is they are sitting on hot money. They are catering to people who want immediate gratification, and more than often the executives themselves seek quick benefits, too. Addicts catering to other addicts don't have the time to do the kind of work that we do. They don't have the stomach to buy assets the prices of which do not currently trend in the right direction. They run after trends and averages and correlations. Sometimes it works, sometimes it doesn't. Nobody knows why. That's not our business.

I read an interview with James Grant years ago. The topic was the value of understanding sound economics. He said, and I paraphrase a bit, that it allows one to navigate inside a dark room because he knows the place and shape of the furniture. Indeed, what a great answer, I thought. So, one last question: You take your scholarly understanding of theory and history and you put it within the constraints of making actual decisions that affect other people's savings. How do you see the application? Is it easy? Is it hard?

I think the role of economics is even more limited. Let's stay in that metaphor. Then the economist is not the one who could tell you anything about concrete shapes and places. He would not even know what furniture is. But he knows that space has three dimensions, that there are physical objects and that they extend in space, that all such objects have causes and effects, and that you should better not try to walk through a wall. This is not much. But in a dark room filled with claustrophobic and frightened people, who are growing mad, and who start imagining objects without causes and actions without consequences, having someone like that metaphorical economist can be quite useful and even vital. Now, returning to real economics, it is truly a wonderful discipline, the queen of the social sciences. But like all sciences, all it can ever give us is partial knowledge about various facts and causal relations that remain constant in time and which are often known in advance. It tells me that the money supply always and everywhere has a positive impact on the price level, and technological progress always and everywhere a negative one. But it does not tell me how these two factors will combine in any concrete situation in the future. It does not tell me how high the prices will be that *my* firm will have to pay next week for its supplies, or will obtain next year for its products. It does not tell me what I should do here and now, faced not only with eternal truths, but with various short-lived realities bearing on this fleeting moment in time, and on all the subsequent ones, that I must go across to reach my goal. The problem of decisionmaking is to cope with all of this, to act in the midst of the transient and of the unknown. That’s definitely not easy.

I truly thank you for your time and your insights. ✦