Ronald Stoeferle – The Matterhorn Interview Jan 2016

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"The Matterhorn Interview – Jan 2016: Ronald Stoeferle"

This late January interview that Lars Schall did with Incrementum Investment manager Ronald Stoeferle comes shortly after the December launch of Ronald's book 'Austrian School for Investors' **co-authored with Mark Valek and Rahim Taghizadegan**. The podcast interview deals with this year's prospects for gold, silver and mining shares, the ever increasing gold appetite in China; and about the new book. To get your copy [English/Dutch versions] please visit the link below the transcript.

Podcast interview: (30 mins)

"2016 WILL BE A GOOD YEAR FOR GOLD INVESTORS"

https://youtu.be/ocRbHD6_iOQ

Transcript

LS: Let us talk about your optimism for gold in this year. In the summer of last year, we were talking in Vienna about "Waiting for Godot", which you brought into discussion with regards to the delayed interest rate hike. In the meantime, the Federal Reserve in the United States has raised rates. Does this mean Godot has finally arrived on stage?
RS: It has but it will leave the stage probably very soon. I think the Fed has made a major mistake not raising rates much earlier and I think now they've basically had to raise rates just to show that they have still got some credibility. However, the rate rike will be a "one and done". I am absolute certain, that the Fed will sooner or later have to reverse course. At the moment, the Fed still confirms that there might four rate hikes this year but I totally rule that out and in fact the market is ruling it out as well.
From my point of view, odds for a recession in the US are increasing every day. I think it will happen. I think equity markets are probably the best forecaster of economic growth. And we all know how weak the stock market looks these days. Under the surface, market internals showed us already in summer that we might enter a bear market soon and now even the FANG-stocks got trashed…

Moreover, most economic data came in much weaker than expected and therefore a US recession in 2016 is highly likely. Now we all know what central banks do when a recession comes; they're printing money,. They will embark another round of QE and I also do not rule out negative rates in the US. In fact, Kenneth Rogoff, the star economist from Harvard, just mentioned in a Bloomberg interview in Davos that the Fed should consider negative rates, and therefore I think it's going to be a very, very interesting year for gold investors and for macro investors in general.

LS: Yeah, and if the Federal Reserve has indeed to back pedal, what effect would this have on gold?
RS: I think gold is already kind of pricing that in, as it held up very well recently. Everybody was scared of this rate hike in the US, so everybody thought that gold would get slaughtered after the rate hike but it was a classical 'buy the rumor, sell the fact'.

LS: Mhm.
RS: Also, from a technical perspective, gold looks very, very positive. I think that the pessimism regarding gold, having a look at the consensus data is already dead negative. There are probably more grizzly bears in Austria than gold bulls on earth.
Having a look at the positioning based on a commitment of traders' report, it looks very encouraging, and moreover I always said that stock markets are more or less the opportunity costs for gold, so as long as stock markets are reeling, gold has got a tough time. Gold performs really well when equity markets are struggling. That's exactly what we're seeing and as soon as the market price is in perhaps negative rates in the US or a fourth round of quantitative easing, I think that gold will then really pick up momentum. Yeah, therefore I think it's going to be a good year for gold investors at least.

LS: Would you say it is important to have a calm gold price, a not too volatile gold price in particular to the upside in order to keep interest rates low?
RS: Yeah. I mean, we have already talked about manipulation and intervention of gold prices quite a lot, Lars, as you know, and I think of course there are interventions happening in gold but there's massive interventions happening in every market these days, so we are far away from a free market.

LS: Yes, but it started, I think, with the gold market.
RS: Yes, of course, because Gold – still – is in the center of our monetary and financial system! Gold is the thermometer of currencies and therefore of course central banks do not want a rapidly rising gold price. I think that we have seen in the last one or two years that gold did very well in many currencies, actually in Euro terms, gold was up, I think, 12% in 2014, it was flat in 2015. Gold is on a new all-time high in South African Rand. It's developing really nicely in basically every emerging market currency. It's doing very well in Canadian Dollar and Australian Dollar but not in US Dollar terms. So, we have to ask ourselves, what's the basis for the strength in the US Dollar, and I think that the narrative is that everybody expects the Feds to continue raising rates. Everybody thinks that economic numbers in the US are better than the rest of the world and I highly doubt that. I think the

market will start realizing that the emperor has no clothes. And that should be quite good for gold.

LS: We've also discussed last summer in Vienna the silver-to-gold ratio, to which you pay attention to. How has this ratio developed in the meantime and what are the conclusions to be drawn?
RS: The gold/silver ratio is really crucial for everyone interested in gold, but also in inflation. Now, as expected, the gold/silver ratio has risen. At the moment, it is at 78 – so one ounce of gold buys 78 ounces of silver. Why do we put so much emphasis on the gold/silver ratio? Because, first of all, we did quite a lot of numbers crunching on that and it clearly shows in times of this inflation or deflationary pressure, the gold/silver ratio is rising because silver has got a high industrial demand. So, if we're experiencing disinflationary times, silver actually struggles much more than gold. Now, of course at the moment, we've got massive deflationary pressure.
Just have a look at industrial commodities; have a look at agricultural commodities, have a look at oil prices especially, but also from this asset price inflation that we saw over the last few years. The Fed always talks about the so-called wealth effect, so the stock markets and real estate is rising, everybody is feeling more confident in the economy and spends more money. Now, in theory, that works but if asset prices are falling, you've got this wealth effect in reverse, so this is also having deflationary pressure, and actually the gold/silver ratio did exactly what we expected it to do. It was rising so as soon as the ratio is falling, that means that inflationary forces are getting stronger again, but at the moment, we are far away from that.
However, we know that due to our monetary system and of course due to the enormous amount of debt, we just cannot afford deflation, so I think central bankers are getting really nervous these days and sooner or later, they will implement massive inflationary policies, like another round of quantitative easing perhaps. Governments will step in with massive fiscal stimulus, people's QE, something like that will have to happen sooner or later unless we see a deflationary bust like 2008. From my point of view, the chances are really high that something like this is going to be introduced in the next few months.
Another interesting finding of our research is the fact, that the gold/silver-ratio is a great confirmation indicator. It's a very good confirmation for gold because what you really want to see in a strong bull market for gold if gold is picking up momentum, you want to see silver actually outperforming gold. So, it's a very easy ratio but there's a tremendous amount of information in this gold/silver ratio.

LS: Let us talk about another ratio. You've mentioned the plunging oil prices as a deflationary signal. Now, you pay attention to the gold-to-oil ratio. Can you talk a lot about this please?
RS: Yes, of course. I mean, we all know that gold is not a commodity but gold is a currency, probably the most solid and reliable currency in history, and we also know that oil is still the most important commodity. Having a look at the long term relation between gold and oil, you can tell that being invested in gold, having gold as your currency, you've got a very stable purchasing power measured in oil, but at the moment, it's obvious that the ratio has

risen dramatically, so your purchasing power in relation to oil has basically exploded.
Going back into history, you can see that every time that this ratio when it’s so high, it was a time of massive crisis. We had the same with the European debt crisis in 2011. We had the same in 2008. Basically we had the same in 1997 with the Asian crisis and before with the Latin American crisis. So, this ratio perfectly shows you times of stress in the system and at the moment, I think there’s enormous stress in the system, especially the large oil producers that developed huge sovereign wealth funds in the last years…

LS: And what about China?
RS: I think that what’s happening at the moment, we already wrote a guest commentary in the Neue Zurcher Zeitung in fall, in October, about China, and from our point of view, it’s not the issue if they will see a soft or a hard landing, but we’re seeing an enormous credit bubble collapsing in China. And this is the major cause for many problems that we’re seeing at the moment.

LS: Yeah. Do you think this will lead to an even larger increase of gold demand in China?
RS: I think so because as we know, stock markets are struggling in China and a whole generation of Chinese stock market investors probably will never buy equities again, as they have completely lost trust in the last few months. Chinese government implemented the circuit breaker which made it even worse of course. We are going to see much more capital controls, in fact everybody is expecting the Chinese government to devalue the Renminbi sooner or later, and they will because of their pact to the US Dollar, they imported a very, very strong currency, and of course, that’s a competitive disadvantage to their Asian neighbors. So, they will devalue their currency big time – and against what should they devalue? Of course, they will also devalue against gold. So as we can already see, gold demand from China is picking up significantly and I think this is going to continue.

LS: Also last summer, the Chinese said what they officially hold in reserve in gold, I think it was something like 1,700 tons. Do you think this is accurate or would you say that you think it is much more?
RS: R: Well, I think the Chinese… I wouldn’t trust Chinese numbers in general. We all know how they are calculating their economic numbers and if they want to see 7% growth, they will publish 7% growth, so I would take the numbers of their gold holdings with a grain of salt. I think there are several institutions in China actually holding gold so it’s not only the People’s Bank of China, the Sovereign Wealth Funds and so on that can hold gold. What we’re seeing is that they’re constantly adding up to their reserves.
That’s definitely a strong sign, but I wrote in my last report that I do not believe the narrative of the market that the Chinese want to really peg the currency with gold because what would happen if the Chinese would have a gold pegged or a gold-backed Renminbi? It would be enormous pressure on the Renminbi actually on the upside and the Chinese, as we know, due to their economic numbers these days, they don’t want to see a strong currency, and we should not forget that it’s also essentially a planned economy and central bankers and the government would have much less leeway and flexibility if the

Yuan would really be pegged to gold.
So, perhaps what Willem Middelkoop said quite recently might be accurate that it’s really a long term story and that the Chinese want to have the leading currency only in 2049, or something like that. I don’t think it’s going to happen tomorrow. I think this is a very long term story and of course gold is a part of that long term strategy but I just don’t believe this narrative that they now want to have a gold-backed currency.

LS: What are your expectations with regard to the development of mining shares this year?
RS: Well, we have seen an enormous amount of wealth destruction within the sector. People have completely lost faith in mining stocks. I think it’s the most hated asset class these days. I don’t know what the current number is, because the last few days have been very weak, but a couple of weeks ago, the total market capitalization of the 16 biggest gold and silver miners was roughly 50 billion US dollars, so that’s quite a low number if you compare it especially to all of those fancy internet and social media stocks these days. I think that the sector really did its homework and lot of positive things happened. They wrote off projects, they really cut their costs, and they’re focusing on cash flow again, so I think from a contrarian perspective, it’s a great buy these days. However, those companies just need a rise in gold price. If the gold price goes flat or even lower, they will really have a hard time, and I cannot rule out that some of the bigger miners will go bust sooner or later because they’re heavily indebted. However, we are having quite a lot of very interesting companies on our watch list. We’re going to invest in them as soon as our inflation signal shows rising inflation again, and I think those companies are real bargains these days.

LS: Now, talking about investing, last month a book was published, which is called ‘Austrian School for Investors – Austrian Investing Between Inflation and Deflation’. You are one of the authors. Please let us know about this. Why did you write this book? Were you in need for money?
RS: (Laughing) I think if you really want to make money, writing a book is probably the most stupid way to earn any money – if I would calculate our hourly salary, I think I would shoot my head. No, we just wanted to get our view out on investing and it was basically also the reason why I quit my job at the bank. I think, we’re not in a cyclical crisis, we’re in a systemic crisis – and the Austrian School of Economics really focuses on those systemic problems; on monetary inflation, on the consequences of fiat money and so on, and therefore I think for an investor, this gives you a tremendous advantage to 99% of investors.
I think there’s a major opportunity knowing about the Austrian Business Cycle Theory; knowing about this interplay between inflation and deflation, and therefore my partner, Mark Valek, and I, we are managing our funds together, and Rahim Taghizadegan, who is the founder of the Institute for Value-Based Economics here in Vienna, we wrote the book in German. It came out one and a half years ago and it was a huge success. I mean, we didn’t sell as many copies as Harry Potter or 50 Shades of Grey but still I think for such a niche, it was quite a big success.
And then we said, “Okay, we have to translate it into English”, because there are only a few books about Austrian investing available. In fact, there’s one

by Mark Spitznagel, it's called 'The Dao of Capital'. Spitznagel was the partner of Nassim Taleb and they managed funds together. And there's one called 'A Viennese Waltz Down Wall Street' by Mark Skousen. But besides that, there are no books on Austrian investing. Our book is a huge success in the English speaking world too. We're getting very, very positive reviews, sales numbers are good.

LS: No, but let us talk then about Austrian investing. Can you describe the philosophy?
RS: Well, there are many, many conclusions of our book and many people say that it's actually quite a philosophical book, so we're not giving specific investment recommendations like 'buy this stock or this bond or this fund', or whatever. I think first of all when it comes to Austrian investing, what I already said is the Austrian School is focusing on our monetary system and its consequence. From an Austrian perspective, monetary inflation always leads to asset price inflation and sooner or later price inflation. This is the root cause of all evil. However, in the mainstream world, inflation always means rising prices. So, Austrians do not regard inflation as an increase in the price level but it means a rising money supply.
Now, I think what is really important when it comes to the Austrian investment philosophy, the Austrian School is very humble so they're saying, "We cannot foresee the future. We have to get ready for all possible scenarios", so diversification is very important. Of course, value investments are within this Austrian investment spirit and the Austrian School puts a great emphasis on the entrepreneurial spirit. In fact, Ludwig von Mises I think once said that the entrepreneur is the historian of the future which I think is a really great description. Moreover, the Austrian School says that saving is actually something really, really positive although nowadays hoarding or saving is something bad because of our interest rate level, but there has to be saving then investment then consumption and not the other way around. I think that the beauty of the Austrian School these days is that a good investor really differentiates themselves from bad ones in a time of crisis.
So, at the moment, I think it's really hard for every investor because nobody really knows how it's going to proceed but the Austrian School was founded and developed during a time when monetary reforms, hyperinflation, wars, financial repression and so on were quite common. So, the Austrian School doesn't really care, you know, calculating GDP and forecasting GDP; is the US economy going to grow 1.2% or 0.9%? That's absolutely useless. The Austrian School really helps you to understand the big picture and I think this is what's really crucial these days.

LS: Is gold in the center of the book? I could imagine it as some kind of twin of debt, you know, as the opposite of debt as a financial asset with no counterparty risk.
RS: Of course, of course. Gold is really central but that doesn't necessarily mean that every Austrian minded investor has to be a gold bug. Of course, people understanding the Austrian School, they've got a different view on gold and they know that during history, market participants always came back to gold in times of crisis or to back a new currency, but as I've said, it doesn't necessarily mean that you should put all your eggs in one basket.

I think that one advice that one can make based on the Austrian investment practice is avoiding large losses is crucial these days. Of course, diversification and having as many uncorrelated assets as possible is crucial. Moreover, we have to focus again on real returns because, from our point of view, stagflation is a scenario that will happen sooner or later, and therefore I think that the proportion of gold in your portfolio perhaps should be roughly equivalent to the expected probability of the occurrence of extreme scenarios. So, if you think that we'll see hyperinflation, monetary reform, whatever, if you're absolutely certain about it then of course you should hold a much larger amount of gold in your portfolio than if you think, "Okay, it's going to be bad', perhaps there will be some inflation, some price inflation and continued financial repression but there's not going to be hyperinflation then you should hold with less gold. So, I think Roland Baader once said it brilliantly; you should keep one third of your portfolio as if it were good times and one third as if it would be normal times and one third as if it would be horrible times.
I think that's very, very simple advice but the beauty of the Austrian School is its very intuitive. We often meet very successful entrepreneurs and when you say, "Oh, do you know the Austrian School?" "No, I've never heard about that and I actually don't care about economics", then you're telling them about the basic principles and they say, "That's exactly what I always thought because we just cannot go into more and more debt and expect that everything will work out just fine". That's not going to work, not in theory and not in practice. Yeah, I think the book is hopefully an interesting read, very thought provoking, and therefore I hope that the English version is also going to be quite a success.

LS: Yeah, I wish you nothing but success and also personally for 2016. Thank you very much for this interview.
RS: Thank you very much, Lars. As always, I really enjoyed it and all the best to you and your listeners.

Ronald-Peter Stoeferle*, who is a Chartered Market Technician (CMT) and a Certified Financial Technician (CFTe), was born October 27, 1980 in Vienna, Austria. During his studies in business administration and finance at the Vienna University of Economics and the University of Illinois at Urbana-Champaign in the USA, he worked for Raiffeisen Zentralbank (RZB) in the field of Fixed Income / Credit Investments. After graduating, Stoeferle joined Vienna based Erste Group Bank, covering International Equities, especially Asia. In 2006 he began writing reports on gold. His benchmark reports on gold drew international coverage on CNBC, Bloomberg, the Wall Street Journal and the Financial Times. Since 2009 he also wrote reports on crude oil. In 2013, Stoeferle and his partners incorporated Incrementum AG in Liechtenstein, where he manages a fund that is managed based on the view of the Austrian School of Economics.*

If you are interested in reading the first true compact yet complete version of what Austrian economics is about get your copy right now before it sells out. **Worth every penny**. To purchase "Austrian School for Investors". **Please click here and understand where Dr. Ron Paul found his political ethics**.