New World Money

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Chapter 1:
Bitcoin Rises From the Ashes

You are looking at a live picture of Lehman Brothers' 158-year-old firm—born pre-industrial revolution and surviving the Great Depression...

Lehman Brothers will file for bankruptcy this evening under circumstances that, without the government's assistance, sources tell us would almost certainly result in significant market disruption.

– CNBC special report, September 14, 2008

I trust you remember what happened next.

The credit market's liquidity evaporated. The S&P was cut in half. 30 million jobs were shed. U.S. households lost $16 trillion worth of financial wealth. More than one million homes were lost in foreclosure.

Fear and panic spread. Some said the stock market was going to zero. Some said this was the end of capitalism. Others said it was the end of human civilization.

The U.S. government rushed in with a $700 billion bail-out package for banks it deemed "too big to fail." With the stroke of a pen, taxpayers were on the hook for Wall Street's reckless behavior.

But it didn't stop at $700 billion.

The Federal Reserve (the Fed) went on to inject $3.7 trillion into the financial system over the next several years.

The Fed used this new money to do two things.

First, it purchased U.S. Treasury bonds in bulk to artificially suppress interest rates.

Second, it purchased the toxic mortgage debt from Wall Street, thus transferring bad debt from the banking sector to the public sector... to the taxpayer.

This was sold as heroic. Fed Chairman Ben Bernanke called it "The Courage to Act" in his memoir.

But a few people out there weren't so sure. They had to ask: Where did that $3.7 trillion come from?

And the answer they found was rather simple. It came from nowhere. Well, to be more specific, it came from a journal entry on the books of the Federal Reserve.

The Fed is very honest about how this works. They tell you right on their website. The Fed basically writes a check "against itself" to create money for whatever purpose it deems necessary.

Now most people don't question this. It's not even on their radar. But those who understand basic economics realize something very important: Value is driven by supply and demand. As supply goes up, value tends to go down.

In other words, an item needs to be relatively scarce and relatively useful for it to have value. This is true of anything... especially money.

The median household income in the United States is about $53,000 per year according to the U.S. Census Bureau. You need at least six decimal points before your Excel spreadsheet can compare

this $53,000 figure to the $3.7 trillion that the Fed created from nothing.

What does that say about your monetary system?

This caused a few people to protest the Wall Street banks. And a few others protested the government.

They learned pretty quickly that their protests were doomed from the beginning. Brute force and opposition is not what changes institutional systems.

Systems theorist Buckminster Fuller observed this dynamic early in the 20th century. Here's Bucky:

> *You never change things by fighting the existing reality. To change something, build a new model that makes the existing model obsolete.*

But this was not a new discovery.

Famed artist Michelangelo understood this way back in Europe's High Renaissance period. "Criticize by creating" is how Michelangelo put it.

Let's turn our attention back to 2008.

Lehman Brothers has collapsed. Wall Street is in shambles. Fear and panic is spreading across the country… and across the globe.

In this environment, a curious message appeared on an obscure mailing list dedicated to the study of cryptography. The date was November 1, 2008. The author was Satoshi Nakamoto.

> *I've been working on a new electronic cash system that's fully peer-to-peer, with no trusted third party… The main properties:*

Double-spending is prevented with a peer-to-peer network.

No mint or other trusted parties.

Participants can be anonymous.

New coins are made from Hashcash style proof-of-work.

The proof-of-work for new coin generation also powers the network to prevent double-spending…

I had to write all the code before I could convince myself that I could solve every problem, then I wrote the paper… You're already right about most of your assumptions… Governments are good at cutting off the heads of centrally controlled networks like Napster, but pure P2P networks like Gnutella and Tor seem to be holding their own…

Bitcoin was born. It rose from the ashes of the worst financial crisis since the Great Depression.

But to truly understand bitcoin, the world's first digital currency (or cryptocurrency), you must also understand money. What is it? Where does it come from? Where has it been?

Think about it. What is money?

We know what money does—it buys things. But can we define it?

Is it a green piece of paper with numbers, words, and symbols printed on it? Is it a card with your name, a string of numbers, and a bank logo on it?

Or is that just a piece of paper and a piece of plastic?

The short answer is that money is a unit of account that serves as a medium of exchange. But this is an incomplete view. To be sustainable, money must have several definitive characteristics.

- **Money must be durable.** It must serve as a store of value over long periods of time.
- **Money must be portable.** It must be easy to move money around—either in person or electronically.
- **Money must be divisible.** You must be able to break money down into consistent smaller units that add up to consistent larger units. In other words, you must be able to make "change" out of your money.
- **Money must be fungible.** It must be interchangeable. Each monetary unit must be consistently the same.

Any item that has these properties can serve as money.

Now that we know what money is, we need to figure out where it comes from… and where it has been.

As it turns out, this story is far more interesting than you would think.

A Brief Monetary History

Prior to the 20th century, most of the world operated on the gold standard through which international trades were settled in gold.

While not perfect, the classical gold standard kept nations mostly honest in their financial dealings with each other. It also forced nations to live within their means.

Large trade deficits had to be settled in gold, which drained gold from the nation's reserves. Conversely, a trade surplus added gold to the nation's reserves. This system placed limits on national debt.

World War I effectively put an end to the classical gold standard in 1914. To finance the war effort, the countries involved "printed" new money that was not convertible to gold. Trade settlement in gold was suspended indefinitely.

Most nations attempted to go back to the gold standard once the war was over. But the excessive money-printing caused their national currencies to diminish in value significantly. That meant nations would have to peg their currency to gold at a higher ratio than before, thus admitting the currency had lost value. Instead, the war combatants scrapped the gold standard.

During the same period, the shift towards central planning in America led to the creation of the Federal Reserve System in 1913.

The Federal Reserve is not a government agency. It is actually a group of private central banks that act as one unit. The U.S. government granted the Fed a legal monopoly on the issuance of currency.

In other words, the Fed is permitted to create U.S. dollars as it sees fit. Anyone else who attempts this will go to jail for counterfeiting.

The Federal Reserve was also tasked with being a "banker's bank," which meant the Fed would loan newly created money to commercial banks that got in trouble. They thought this would make the system stronger.

Instead, it created "moral hazard" within the banking system. Commercial banks knew that the Fed would bail them out if needed... so lending standards diminished over time. It became easier and easier for risky borrowers to get a loan.

This is the dynamic that ultimately caused the financial crisis of 2008. Wall Street, backed by the Fed—and the government—made too many loans to too many risky borrowers. Then it chopped up those risky loans and packaged them into complex derivatives.

And they kept doing this until it all blew up in 2008.

Rather than learn their lesson, the monetary authorities transferred the banking losses to the public with bailouts and quantitative easing programs to keep the system going.

But we need to back up for a minute. Those bank bailouts and quantitative easing programs would not have been possible 100 years ago. There were several changes to the monetary system that had to occur first.

The U.S. dollar was backed by gold when the Fed was first created in 1913. Americans could trade their dollars for gold anytime they wanted to at first.

But then, in 1933, President Franklin Delano Roosevelt (FDR) issued an executive order that made it illegal for Americans to own gold. In fact, Americans were required to sell their gold to the government for $20.67.

After it had bought all the gold domestically, the U.S. Treasury announced that foreign central banks would still be able to trade dollars for gold… but it raised the conversion rate to $35 per ounce.

This influx of gold for cheap gave the U.S. government a strong seat at the Bretton Woods conference in 1944. At this conference, representatives from 44 nations met in Bretton Woods, New Hampshire to discuss a new international monetary system.

They agreed upon the “Bretton Woods System” that established the U.S. dollar as the world’s reserve currency.

As the world’s sole reserve currency, the dollar replaced gold as the medium for international trade settlement. This meant that all international goods would be bought and sold in U.S. dollars… no matter which nations were doing the buying and selling. The dollar would remain pegged to gold at $35 per ounce, and other nations could redeem their dollars for gold through the “gold window.”

The dollar's convertibility into gold on demand was to serve as a "check" on the United States. The link to gold is what gave the other countries confidence in the U.S. dollar.

The Bretton Woods System bestowed an enormous privilege upon the United States because it created a global demand for dollars. All nations needed to hold U.S. dollars to facilitate foreign trade.

This dynamic made trade deficits irrelevant for the United States. Under the gold standard, trade deficits required the U.S. to send its gold to another country. Under Bretton Woods, trade deficits required the U.S. to send its dollars to another country. And the U.S. could just print new dollars to ship out if it needed to.

This artificial global demand for dollars is what powered Lyndon Johnson's "guns and butter" campaign that ramped up in the 1950s.

The U.S. military went to war with Korea and Vietnam overseas. That was the "guns" part. At the same time, the Great Society welfare programs launched domestically. That was the "butter."

These initiatives were extremely expensive. As they progressed, the U.S. government created more and more new dollars to pay for them.

But foreign countries took notice. They began to worry about the value of the dollars they were holding. And rumors of the U.S. unilaterally changing the gold conversion ratio spread.

Here's former French President Charles de Gaulle in 1965:

> *The fact that many countries accept as principle, dollars being as good as gold, for the payment of the differences existing to their advantage in the American balance of trade... this fact leads Americans to get into debt and to get into debt for free at the expense of other countries... We consider necessary that international trade be established*

as it was the case before the great misfortunes of the world, on an indisputable monetary base, and one that does not bear the mark of any particular country. Which base? In truth, no one sees how one could really have any standard criterion other than gold!

France and other concerned nations began to rapidly exchange their dollars for gold through the gold window. It was a global "bank run" on the dollar and gold rapidly flowed out of U.S. vaults.

By 1971, the U.S. Treasury only had enough gold to cover 22% of all dollars outstanding. It was about to run out of money.

The Birth of the Petrodollar

On August 15, 1971, President Richard Nixon closed the international gold window to stop the outflow of gold. Nixon assured the world that this closure would only be temporary.

"Your dollar will be worth just as much tomorrow as it is today," Nixon proclaimed on television with a straight face. "The effect of this action, in other words, will be to stabilize the dollar."

But Nixon had a trick up his sleeves.

Along with his Secretary of State Henry Kissinger, Nixon struck a deal with the Saudi Royal Family. The Saudis agreed to price all international oil sales exclusively in U.S. dollars. They would refuse settlement in all other currencies. In return, the U.S. would provide military protection and military-grade weapons.

This deal effectively kept the U.S. dollar as the world's reserve currency, even with the breakdown of the Bretton Woods System.

By 1975, all OPEC nations followed suit and agreed to settle oil trades exclusively in dollars. These were the largest oil producers in the world, and they only accepted dollars. Which meant all other countries still needed to obtain dollars to purchase oil.

This is where we stand today.

We are in the midst of a global experiment with fiat money.

Since 1971, the U.S. dollar and all other currencies have been *created from nothing by government decree*. That is the definition of “fiat” currency.

All restraints on currency creation have been removed.

It took a little while for governments to catch on. But throughout the 1980s, national governments realized they had unlimited money to spend.

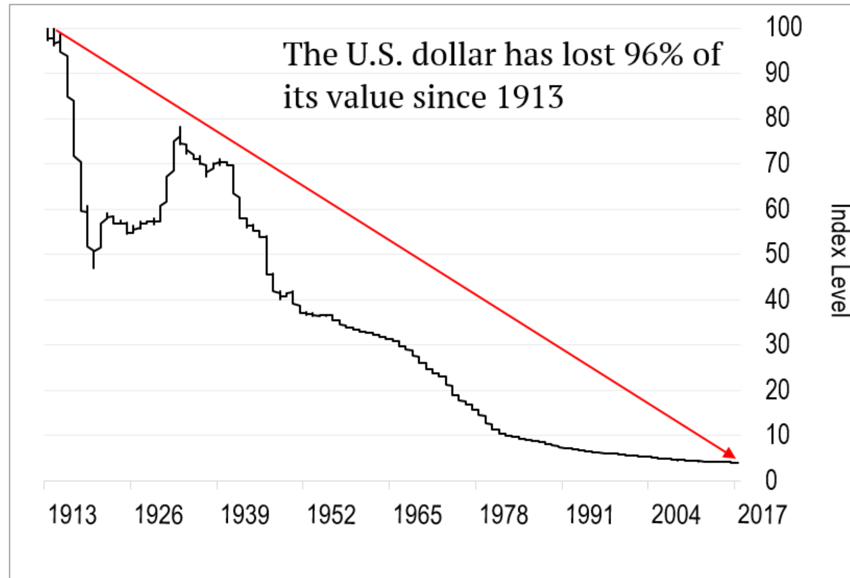
And spend they did.

But their money-for-nothing policies were not without consequences. Prices for goods and services exploded across the board as new money flooded into the economy.

That is why the hamburger that cost $0.45 in 1971 costs $5 today.

The obscured fact is that this is not a case of rising prices. Your dollars are actually losing value over time—thus requiring more dollars to buy the same item. Price inflation is an artificial monetary event.

To come full circle, the U.S. dollar has lost 96% of its value since the Federal Reserve opened its doors in 1913. Stated another way, the dollar could purchase nearly 50 times more goods and services back in 1913 than it can today.



Despite Nixon's proclamation on national television, the value of the U.S. dollar fell off a cliff.

While incomes in general have also risen during the last 100 years, their rise has not kept pace with the dollar's loss of value. This is the primary reason households now require two wage earners to make financial ends meet.

The global experiment with fiat money has also led to an explosion of debt, especially in the Western economies and Japan. Without sound money restraint, nations have been able to finance deficits and run up enormous debt that can never possibly be paid back.

The United States' national debt has now eclipsed $19 trillion.

Here is the numerical representation of the U.S. debt:

$19,000,000,000,000

This is an incredible amount of money, especially given we are talking about the issuer of the world's reserve currency.

And it is not just the U.S. Every major country in the world has run up its sovereign debt bill significantly over the last thirty years.

On the Hook for $200 Trillion

But sovereign debt is only part of the story, and a sticky part at that.

Governments accumulate sovereign debt when they issue bonds… which, in the United States, is done through Treasury auctions.

The U.S. Treasury sells notes and bonds of various durations (2, 3, 5, 10 and 30 years) at "auction." The bonds are sold at a "market" rate of interest where the Treasury promises to make interest payments to the bondholder semi-annually for the length of the term, and then re-pay the principal balance upon maturity.

Here's the sticky part: National governments can easily "roll-over" their outstanding debt by issuing new bonds to pay off the old bonds when they come due. If market demand for the new issue falls short, the central bank can simply create more dollars to buy the new bonds.

That is the magic money machine. And it is how they kick the debt can further and further into the future.

Here's the other part of the story: unfunded sovereign liabilities far exceed sovereign debt around the world… especially in the U.S.

Unfunded sovereign liabilities are future expenses that governments have already committed to paying. The biggest of these are pension plans and health care programs—Social Security and Medicare in the U.S.

Generally Accepted Accounting Principles (GAAP) require private companies to report unfunded liabilities in their financial

statements… but government gets a pass. So, you won't find these listed on any government balance sheet.

Boston University economist Laurence Kotlikoff estimates U.S. unfunded liabilities to be $222 trillion. The bulk of this comes from Social Security and Medicare.

It wasn't always this way. Social Security was solvent in its early years.

And it was a great deal for a lot of people who retired in the early stages of the program. Take the story of the first Social Security payee, Ida May, for example.

Ida paid a full $24.75 into the system before retiring. She lived to receive nearly $23,000 in retirement benefits. No one thought twice about this at the time because there were 42 workers for every person receiving Social Security benefits.

There are now 2.8 workers for every Social Security beneficiary. Simply put, there are no longer enough workers to pay for retirees. The difference is the unfunded liability.

Social Security is already running a $50 billion deficit annually. That is with most of the Baby Boomer generation still working.

This annual deficit will grow larger and larger as the Boomers retire. And demographics show that there will be 10,000 people in the United States turning 65 every single day for the next decade. That's a whole lot of people knocking on Social Security's door.

The Medicare system is not doing much better. Medicare is currently running a $30 billion deficit annually. Again, that deficit will grow larger as the Baby Boomers retire.

I am highlighting the U.S. government simply because of the dollar's supremacy in global finance. But they aren't the only culprits. Most developed nations have accrued unfunded liabilities to some degree.

The Magic Money Machine

Free market economists have been decrying this system since it came about with the Nixon shock in the 1970s. “It will never work,” they said. “The feds will destroy the currency.”

But the fiat money system is still chopping along nearly 50 years later. Fiat currencies have plummeted in value since this experiment began in 1971. But they haven’t died.

The old free market economists could not foresee how the central bank would be used to crank out new money and lock away bad assets. They underestimated the power of the magic money machine.

Or perhaps they just confused inevitable with imminent.

The magic money machine cannot reverse course. The debt and unfunded liabilities accumulated can never be paid off. They can only be “rolled over” by creating more money and more debt. This guarantees that fiat currencies will continue to lose value every single year.

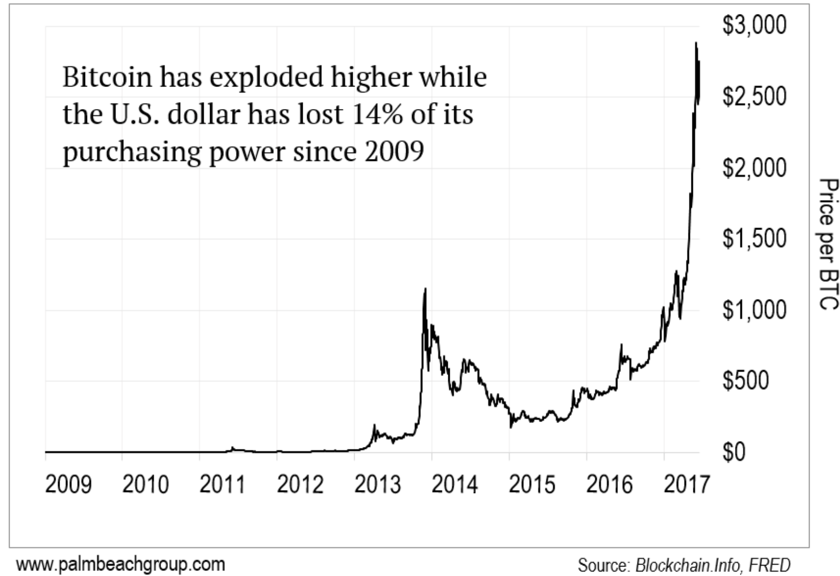
Which means the money you work so hard for will constantly lose value… forever. The magic money machine will never stop stealing purchasing power from you…

Up until 2009, there were no alternatives to this system. You were stuck holding paper money that was depreciating by the day. You were trapped in the rat-race.

No longer.

Bitcoin gives you a way out. With bitcoin, you can exit the abusive fiat money system. You can hold money that will grow in value over time because it is extremely scarce. And you can stop the magic money machine from stealing the value you work so hard to earn.

Bitcoin Since 2009



The abusive fiat money system creates a world in which you must work harder and harder just to maintain the same standard of living. It is impossible to save money because that money constantly loses value.

Bitcoin reverses this dynamic. It allows you to truly reap the fruits of your labor. And bitcoin makes it much easier to maintain, or even increase, your standard of living over time.

That is why I chuckle whenever I hear the objection: "But I can't buy my coffee with it."

One day you will be able to buy everything with bitcoin as easily as you swipe your credit card today. But that misses the entire point.

Bitcoin is not here to make shopping easier. It is not here to be a digital version of the dollar.

Bitcoin was born from the ashes of the 2008 financial crisis. It is here to give you a way out of the abusive fiat money system. It is

here to hold the power institutions accountable for stealing your purchasing power. Bitcoin is here to empower you, as an individual.

Bitcoin gives you 100% control of your money. It makes you the President and CEO of your own bank—with all the power and responsibilities that entails.

In a moral system, hard work and dedication should pay off. You should be able to set concrete financial goals and then plan how you will achieve them.

That can't happen when your purchasing power is constantly stolen from you. It certainly can't happen when you are expected to bail-out failed banks and pay off debt you never incurred.

That's why Bitcoin is here—to level the playing field. Ultimately, bitcoin is going to give you back control of your financial destiny.