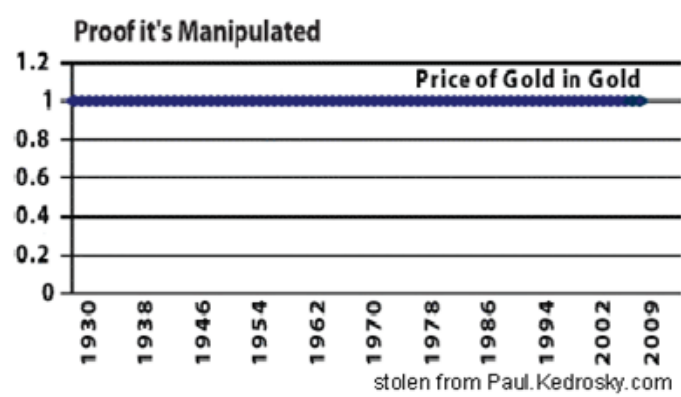


THE VOGUE OF GOLD

An American friend in Vietnam was the first person we know who really got on board the bull market in gold. His explanation for the trade spared us the usual lectures on Austrian Economics, "fiat money" and fractional reserve banking conspiracies that make most gold bugs such incredibly boring dinner partners.

Instead, he just said that Vietnam was booming, alongside China, and that the people there made more than they spent. They saved the difference by purchasing gold, with their local currency. Suddenly it all started to make sense how dollar-denominated gold would rally in price despite what everyone knew were the deflationary risks in the U.S. economy: Because it had more to do with rising Asian savings volumes than the U.S. economy.



And it's not just little Vietnam where savings is preferred in yellow metal. All over booming Asia the story is the same: they don't trust local banks, and they don't trust green paper money. They buy gold. The gold market is driven by private buyers in Asia. The "Belgian dentist" was the image of the eurobond end-buyer in the 1970s, and the gold market's equivalent is an Indian jeweler.

That mistrust of the dollar is by now of course quite widespread. At the APEC meetings in Singapore, U.S. Treasury Secretary Tim Geithner told the assembled crowd of Asian heads of state, finance ministers and other dignitaries that the U.S. "remained committed to a strong dollar." At that point, according to sources in attendance, the room erupted in explosive laughter. You see, they assumed—incorrectly as it turned out—that Geithner surely had to be joking.

Whether that embarrassing episode accounts for Ben Bernanke's subsequent comments on the dollar, unusual for a Fed chairman, is unknown, but clearly Vietnamese savers are not the only ones questioning the dollar's reliability as a "store of value" these days.

The catch of course for gold remains this: What happens if those economies in Asia are actually saving less than they think they are? We all remember the unstoppable Asian Tiger Economies of the 1990s attracting huge flows of hot money, driving up asset values rise in the region, right up until the moment they stopped and the flows reversed.

A glance at the charts shows that 1997, that year of the "Asian Contagion" crisis hit was a very bad year for gold. It declined sharply from already low levels. The question to ask to know if gold will reverse, is not so much whether there is a bubble of retail gold bugs in the U.S. loading up on Krugerrands, but if the money that's been flowing into Asia is becoming a bubble. Are investments being analyzed carefully, or is investment being driven instead by a desire to be invested. The Hong Kong Monetary Authority put out a report today that seems to indicate they're not too sure, and rather worried it's the latter.

Still, the most thought provoking statistic of the week had to be from a Societe Generale report. Their analyst calculated that with the U.S. monetary base of \$1.7 trillion, and 263 million Troy ounces of gold in the U.S. government's vaults, that the dollar could be fully "gold-backed" if the price per ounce rose to \$6,300. We're not sure what that really means in practical terms. Maybe Ron Paul can tell us.

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Please Note:

In observance of Thanksgiving, next week's edition of Policy Insights will be published on Wednesday, Nov. 25.

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