

Investing Through Inflation

Why Gold Was the Bitcoin of
the 1970's

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Why Gold Was the Bitcoin of the 1970's

Summary: *The narrative that Bitcoin is “Digital Gold” has caught the imagination of the investing public. But is it? What does that even mean? This paper compares Bitcoin today to how gold similarly caught the public’s imagination in 1980 when it was the shiny new object of the day.*

There’s a theory that the market you enter at the beginning of your investment career is the market you will trade the rest of your career. If you enter in the midst of a crash you will forever be on guard for a crash. If you invest in the midst of a raging bull market you will forever presume that markets will always, eventually, be bullish. God help those who enter at the beginning of a parabolic market and are cursed to believe that if you can catch just one more wave all will be set right.

What if I had begun my investment career in 2017 right after graduating university? I’d have had a background in maths and computer science with enough business courses to be dangerous. In 2017, at that age with that background, I would most certainly have come across bitcoin. Right at the time when bitcoin was breaking out of the crypto-nerd crowd and into public view.

Bitcoin (BTC) was at the beginning of its parabolic move from \$1,200 to \$20,000. Maybe I would have seized the opportunity and positioned myself to be the go-to BTC expert given my age, my background and the innate ability of a 22-year-old to conflate being involved in the zeitgeist with actually knowing what was going on. Somewhere I would have heard “Bitcoin is Digital Gold” and it would have been a mic drop. Boom! I would have jumped on the wagon and gone for the ride.

I’d like to think my 2017 self wasn’t a complete idiot so when BTC retraced 50% in a quick couple of months thereafter I would have kept my head down. But my commitment would not waiver. This shiny new object, this Digital Gold, would have its day again and I would be there to reap the rewards.

But I didn’t start my career in 2017. I started in 1980. The shiny object of the day in those inflationary times? Gold. Real gold. The 79th element on the periodic table. But how could gold have been the ‘new’ shiny object? It had been used as a currency for a millennium. Why? Because between 1934 and 1974 it was illegal for Americans to own it. For forty years, two generations, nobody in the US knew how to use gold as an investment. Suddenly in 1974 it was released and coincidentally there was inflation and thankfully there was a narrative that gold was an inflation hedge. The fuse was lit but it was a slow fuse.

At year end 1974 the price of gold was around \$100 / oz. Four years later it was roughly \$200 / oz. Not exactly parabolic. Yet.

My career started in the midst of the 1980 great recession. That was when we knew how to do recessions. Deep and long. We didn't invent the word stagflation, the Brits had a decade earlier. But we popularized it. It was a combination that was not supposed to be possible; economic stagnation and inflation at the same time. The working person was squeezed at both ends and interest rates were rising. Enter the shiny new object – gold. The protector from inflation and the store of value. From 1979 to early 1980 the price of gold shot from \$200'ish to \$670'ish – more than a 240% increase. The mania was fed on the hope of riches that would offset the devastation in day-to-day life. It was fed on the historical narrative of inflation protection. There wasn't any recent history of gold to rely on so there was no debunking the narrative.

What's the learning lesson? Be wary of parabolic markets? No – well yes - but no. The lesson is be wary of narratives that cannot be substantiated by historical reason. Inflation in the 70's and 80's wasn't new. There had been bouts after both great wars. But gold wasn't a tradeable asset then. There was no history of freely traded gold during those inflationary periods and there certainly wasn't any history of gold's attribution to a diversified portfolio.

Does that provide a useful analog for understanding BTC? Is there a historical basis to understand if BTC's price is rich or cheap? Is there an understanding of its purpose and its attribution to a portfolio? Be wary of narratives that cannot be substantiated by historical reason.

I entered the industry when gold was going parabolic. Am I intrigued by today's shiny new object that has proven its ability to go parabolic? Absolutely. Yet I keep in mind that after gold's crash in 1980 it took 26 years before gold recovered to its prior peak and it didn't prove to be the inflation hedge the narrative predicted.

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