



## ***DON'T TAKE ANY WOODEN NICKELS***

*July 6, 2006  
Dow: 11,207*

On December 5, 1931 the Citizen's Bank of Tenino, Washington, failed and created a shortage of money. Merchants were unable to get change without traveling about thirty miles over inadequate roads. A meeting of the Chamber of Commerce resulted in the local newspaper printing up the first issue of wooden money in the United States. Other places mostly in the Pacific Northwest issued wooden money after that. Each wooden nickel had an expiration date and even a final redemption time. Eventually, real nickels became available and wooden nickels were relegated to the souvenir bin.

Today because of soaring metal prices, it costs the government 1.23 cents to make a penny. Since 1982 the penny is actually mostly zinc wrapped in copper. Also, it costs the government a nickel to make a dime and less than a dime to make a quarter. Those coins are mostly made of copper as is the Susan B. Anthony dollar. So, today these coins are worth more in paper money than the metal in the coins. That's inflation, and it is caused by the government printing presses. Prior to 1971, we were on a modified gold standard (the Fed was limited in the number of paper dollars they could create). This allowed foreign governments to turn in their surplus dollars for gold. France (our friend?) took full advantage of this to the point of almost wiping out the gold reserves at the US Embassy in Paris. President Nixon was forced to close the gold window. Our link to gold was virtually severed, and since then the Fed has been able to print money in unlimited quantities, and they have. We mentioned in a previous letter that the Fed has stopped publishing M4 and M3 numbers, and M2 is about to follow. Thus we can only guess at the current rate of growth in the money supply.

As we have stated ad nauseam, it is an increase in money supply relative to demand that determines inflation. Interest rates have little to do with it. Paul Volcker, then Chairman of the Federal Reserve, realized this in the early 1980s when he advised President Reagan to ignore interest rates (the prime rate topped at 22.5%) and just tighten the money supply. Market forces will then take care of interest rates. An interest rate of 5.25% or 5.5% or even 6% will not choke off the current economic boom we are undergoing. Today's rates are pretty much the historical norm. We think the

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Fed is more concerned with deflation and are running the printing presses to prevent that. Deflation is occurring in consumer products being imported from Asian countries. This is also being aided by American corporations that are becoming more efficient and competitive. The real inflation in the US is from areas that we cannot outsource and the Fed is aggravating that very inflation with their easy money policies. Remember, inflation is caused by too much money chasing too few goods. Being a millionaire today is not as impressive as it was back in 1970.

Paper money has no intrinsic value. The French were burning paper money during the French Revolution. Confederate money was worthless after the Civil War, and as recently as 1989, East Germans were burning their paper money as the Berlin Wall collapsed. According to the Bureau of Labor Statistics inflation calculator, gold at \$850 an ounce in 1980 (its high) would be worth \$2,100 today. The most important function of a central bank is to maintain a stable value for a nations currency.

Well, another birthday has passed and now the United States is 230 years old – at least from the date of the Declaration of Independence. The war against England and our actual independence did not occur until 1783, and it took some help from our friends in France to accomplish it – imagine that. Well, we returned the favor in the 1940s. In spite of all the problems that the media continues to document for us, we are still the greatest nation on Earth. We have the most freedom, most stable political system (don't laugh) and the highest standard of living on the planet. So Happy Birthday America and many more!

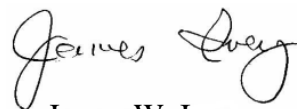
### **Random thought for July 2006:**

“Democracy is the worst form of government in the world – except for all the rest.”

*Winston Churchill*



Michael L. Dana  
Chairman of the Board



James W. Ivey  
President

*Dana Investment Advisors welcomes any comments to their newsletter and is more than willing to discuss or explain any aspect of the letter. Feel free to call us at 262-782-3631.*

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