Demand & Supply numbers in Gold reaching critical levels! Something's gotta give

By Julian D.W. Phillips 1st September 2015

Recent Developments

SPDR gold ETF

In the global gold market there have been ±15 tonnes of gold bought into the SPDR gold ETF.

COMEX

On COMEX we have seen hedge funds and speculators cover more than 125 tonnes of gold short positions but only increasing 50 tonnes of long positions in the last month. More importantly COMEX added 281 tonnes of gold to stock up on gold, available for delivery [as stocks were at very low levels].

Shanghai Gold Exchange

In the world's largest gold market, the Shanghai Gold Exchange, we have seen 194 tonnes withdrawn in the last three weeks, a figure that represents total imports of gold to China and including local production, an annualized 3,233 tonnes.

Demand & Supply totals coming

To put that in context, that represents 111% of newly mined gold production and 75% of total gold supply. After newly mined gold supply, only 'scrap' gold supplies the balance. This is somewhat of a misnomer as it is mainly kept in the family in India. It is also a variable supply, dependent on prices. Now add a conservative 950 tonnes of Indian demand annually [this ignores smuggled gold which is preferred, as it is cheaper but harder to hide in the books, but done] and a conservative estimate of 250 tonnes of smuggled gold and Indian demand is expected to reach around 1,200 tonnes. Chinese and Indian demand then add up to a potential 4,433 tonnes against 4,357 tonnes potential supply. We have omitted U.S., E.U and Middle eastern and the rest of Asian demand usually accounting for up to 50% of demand from these figures.

Liquidity draining

The resulting current shortfall has to be made up with stocks representing the liquidity of the London and New York [and central banks?] markets. While the London market is still very liquid, that liquidity is draining away to the east.

In the past, such a drain was tolerated only for a short time in the face of persistent demand, at which point pricing power goes east! So, how long are gold and silver prices going to remain at current levels?

We are talking of 1975 when first the U.S. tried to squash the gold price with sales of its gold - 500 tonnes [but the amounts on offer were oversubscribed] then the IMF did the same and also found the sale oversubscribed. This showed that while they wanted to crush gold as an alternative to currencies, they were not prepared to get rid of a small proportion of their gold.

It was then they turned to the gold miners and gave them cheap loans of gold bullion to accelerate their gold production by financing such mining with bullion loans, sold forward against repayment in future production. This swallowed up the world's easily mined deposits of gold, which have now gone forever.

As of now with the world, east of Greece, draining gold from the west the gold banking system, alongside the major central banks, are having to supply gold to COMEX and we believe through the London Bullion market as total supplies of gold are insufficient to satisfy total global gold demand.

This cannot go on for long as it also drains the developed world gold markets controls over gold pricing. The western gold market is now faced with either letting Asia dictate gold prices or seeing the liquid gold stocks drained away.

We would expect them to do as they have done in the past and to let gold prices rise to drain off demand in the hopes that such prices can be restrained higher up as demand slows.

Confiscation is getting Closer!

What is most likely to happen eventually, is that as liquidity is drained from London and New York, drastic action will need to be taken to replenish national stocks by drawing off institutional and private gold holdings to replenish government holdings.

This would not just entail taking gold from Custodians, dealers, vaults and other large holders, but prevent local competition from private markets at home from competing for gold against central banks.

Many will say that would not be necessary because such residual holdings would be small. But that's not the point!

The Real Reason behind Gold Confiscation

Listen to Audio:**Audio mp3 of Address**

Many analysts in the past have stated that the real reason behind the confiscation of gold in 1933 was to allow the Fed to increase the money supply through the devaluation of the dollar. This was expressed at the time as a revaluation of gold. Both these statements were inaccurate because of what followed.

Gold was confiscated in 1933 from all citizens leaving them only a tiny amount in their hands. The immediate effect was that dealing in gold [excluding gold with a rarity value] was terminated. Custodians, dealers and institutions found themselves out of the gold business suddenly. This seemed severe, because the vast majority of U.S. citizens had so little gold anyway. So what precipitated these draconian measures?

At the time there was a severe banking crisis which had led U.S. citizens to remove their money from the banks forcing a bank holiday until the many banks in the U.S. could show their balance sheets were solvent. As you can hear in this recording of President Roosevelt's address to the nation at the time the banking crisis was greater than the Lehman Bros collapse in 2008 as it brought banking throughout the U.S. to a halt.

The only alternative to using dollars in the U.S. banking system was gold. Bear in mind 'dollar bills' were backed by gold, but because citizens were allowed to own gold, they had a direct alternative to government/bank issued bills. This was gold itself. If government/banks had lost the confidence of the people, gold still had it. It was this judgemental value of gold that posed a threat to the banking system and dollar bills themselves. It was clear that the banking system and the dollar had a difficult road ahead if gold still stood as an alternative. It had to go. But how?

The easiest and most effective way to eliminate gold as competition to the dollar was to take it away from U.S. citizens and place it firmly behind the dollar. By confiscating gold the Fed had taken all the confidence that gold inspired and placed it behind the dollar, not just eliminating it as competition, but taking its power and reinforcing the dollar and the banking system with it.

Is it any wonder that Roosevelt could then say [in his address] that the banks would be 'lending against 'good assets'?

Today, in the electronic age, governments, through banks, could, if permitted, make society cashless. If they did so, then control over money, the financial system, together with the detail of how all would use it, would lie with government. Could this be the next target of government? Is cash a 'barbarous relic' as the FT stated in a recent article?

In 1974 after 41 years, U.S. citizens were once again permitted to own gold freely. The Gold Standard had disappeared and the U.S. government together with the IMF had banished gold to the role of a reserve asset in the background of the financial system. Its threat was deemed to have ended when Nixon closed the 'gold window' which allowed governments to convert currency outside the U.S. to gold. The dollar gained credibility because it was the only currency in which oil was priced. And everybody needed oil!

<u>But the battle over gold had not been won</u>.

For a start, it remained in vast quantities in the vaults of the Fed and European central banks, none of whom wanted to get rid of their own holdings. Yes, there were token sales from the U.S., from the IMF around 1975, but these amounts of gold were snapped up so fast that it was realized that other nations would take up any further offerings. This century European central banks also tried token sales to eliminate competition to the newly formed euro from gold, but by 2009 as the euro was established, the gold sales terminated. All the gold sold was also snapped up by buyers then too!

All that time, during those years the European central banks reiterated in their statements that "Gold was an important reserve asset". This view continues to this day among all developed and emerging world central banks.

Among central banks gold continues [to quote the then German Bundesbank President] to be a "counter to the swings of the dollar". In other words it remains an alternative to currencies. But this time it is not national institutions or individuals that pose a 'threat to currencies' but other nations. International confidence in currencies by trading partners is now on the decline, whereas the continued qualities that gold provides, outside the suspect national currencies, is not. Gold has no nationality and is free from the constraints that national currencies have in the eyes of other nations.

As with the dollar in 1933 gold is needed to reinforce confidence in all currencies. This means that the larger the gold reserve a nation has, the more confidence it will inspire in extreme times. China's acquisition of gold by the central bank, institutions as well as individuals, reinforces that principle. Russia is hot on its heels.

And this time, no one nation could take gold away from other nations because they only have control over their own Jurisdiction. This means that confiscation of gold outside a national Jurisdiction will not take place by that nation. But pressuring their own citizens and institutions to repatriate their gold [after adding a regulation that they disclose their holdings to government] will be a path governments will follow when they act.

Once gold is seen to be needed to reinforce international confidence in a currency, governments will acquire gold [just as Russia has been doing for over recent years]. As China indicated too, outsiders must take into account local citizen's holdings, when counting a nation's gold reserves. Clearly the government sees it as its right to confiscate citizen's gold for such purposes. While China has been public about it, it is tacitly understood that all governments have the 'right' to do that should they see it a strategically necessary.

The issue of the confiscation of gold remains a threat to private holdings, as both extreme times and waning currency confidence takes hold. Once the Renmimbi [Yuan] is part of a multi currency monetary system the dangers of confiscation grow rapidly. Once one nation takes such a step others will follow. How far in the future will this happen?

Just as it was wise to move out of Europe well ahead of World War 11 to escape the war, so it is with gold now. As in the past, no warning will be given of the intention to confiscate gold. It will happen, likely over a weekend when you can do nothing about it. Likewise, regulations, such as FATCA can be extended to require the reporting of gold holdings just as quickly. Thereafter silence on this by gold owners will be breaking the law.

Let's be clear, just holding your gold outside of your country will not be sufficient. All a government has to do is to regulate that all report their gold holdings to the government. Then it is simple to put citizens under pressure to repatriate their gold. After all, you remain in their Jurisdiction!

Your dealers, Custodians, and storage companies and their Directors will come under the same pressure and are likely to hand over your gold without a fight, likely informing you only after the event. As you will no doubt have found out already, they have no contingency plans to fight confiscation.

What you need is a company that will fight for you and prevent such a confiscation taking the heat away from you. We know of only one [visit the Ultimate Gold Trust through its admin arm Stockbridge Management Alliance Ltd. – ***www.stockbridgemgmt.com***]