

Back in January, I wrote about [the significance of gold breaking above \\$1000 again](#).

Gold

Rising demand for physical gold is a threat to the dollar because it signals a growing loss of confidence in the paper currency. It is also key to understand that gold prices aren't rising because of the changing fundamentals of gold, but because of the changing fundamentals of the dollar. In other words, **gold isn't rallying, THE DOLLAR IS FALLING**.

Gold is history's oldest and most stable currency. Its utility is simply that it is rare, and for 5,000 years people have used it to store value for the future. All the gold that has ever been produced would fit in a solid cube of about 19 meters on each side, and this cube is only expanding by about 12 centimeters a year (2%). Since the value and supply of gold itself are fairly constant over long periods of time, the main driver of gold price fluctuations is the ebb and flow of confidence in paper currencies. Rising gold prices are, therefore, a signal of a weakening currency, which is why governments hate them and [try to suppress them](#).

Right now, there is unprecedented worldwide demand for physical precious metals. As a result of this surging demand, gold futures have [experiencing backwardation](#), a rare market condition where gold futures trade under spot prices. It is a signal that gold prices are headed higher and that confidence in our currency is fading quickly. **When gold prices break above 1,000 again, the event should be recognized for what it is: the herald of a dollar collapse.**

Gold is becoming money once again. The market for the standard gold one-ounce coin [is no longer fragmented](#). Both the ugliest and the most beautiful gold coins are traded strictly by the quantity and quality of metal content, disregarding the outward appearance of the coin. Even Indian gold buyers, who, for years, considered buying jewellery to be the best investment option, are [shifting from buying gold jewellery to gold coins](#).

It has been [more than 40 years](#) since governments and individuals concerned themselves about physically holding gold, but confidence in the dollar is falling and investors are being ["dragged kicking and screaming into the bullish camp"](#) as gold continues to break to the upside.

Gold demand is exploding as Investors turn to gold

Investors around the world are [investing in gold bars for their safety](#). Big investors like David Einhorn are also turning to gold as [an attractive alternative to cash](#), as falling interest rates on savings reduce the opportunity cost of holding gold, a non-interest bearing asset. As Mr. Einhorn put it, "Picking these currencies is like choosing my favorite dental procedure. And I decided holding gold is better than holding cash, especially now that both offer no yield." Finally, a chaotic scramble to secure physical gold has also been unleashed by negative real interest rates (below inflation) which have [upset the gold "leasing" machinery in the gold industry](#), creating a sustained market squeeze.

Surging demand is [spurring a rush at Swiss gold refiners](#), who cannot work fast enough to meet demand. Mints are seeing [a sharp rise in sales this year](#) due to interest so strong that dealers are reported a shortage of products such as Krugerrands and one-ounce bullion coins. One German firm is even planning [gold ATMs to meet growing demand](#), with 500 "Gold-to-Go" ATMs to be set up in Germany, Switzerland and Austria this year.

The rush to buy gold is also filling Swiss bank vaults. Swiss gold ETFs (ZKB Gold ETF - SWX and Julius Baer Physical Gold - SWX) [are moving large quantities of gold out of London and into Zurich](#) (70 tons as of last may), and they are [running out of secure vaulting space](#) (Why doesn't GLD ever have any storage issues? Think about it). This shortage of secure storage extends across Swiss bank system with even gold clearing providers like SIS Clear (who only deals with banking counterparties) running out of space.

China is now the driving force in gold market

China is now the fastest growing market for gold, with [Beijing's gold markets reporting record sales](#). As the Chinese economy rebounds from the global recession this year, China is overtaking India to become [the world's top gold consumer](#). The Chinese authorities are reinforcing this strong demand for precious metals by [pushing their citizens to buy gold](#).

[China's] main state-owned television company is promoting gold and silver as an investment. The government is telling its people to buy gold. What's more, every bank will sell gold and silver bullion bars in four different sizes to individuals, and China's largest bank, the ICBC, is setting up a precious metals department to handle growing investor demand.

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And if the Chinese authorities are pushing gold as an investment to their citizens, it obliges them to 'protect' the gold price, as Lawrence Williams of Mineweb notes. It would be tantamount to a betrayal if it fell, never mind the loss of all-important face that would result. Just as the US and the UK stepped in to bail out its banks, so China will be duty bound to prop up gold.

But the surprising strength we have seen in gold over the summer – we never really got the summer low I was looking for – suggests that somebody is already 'buying the dips' anyway. Indeed, the gold price has this week repeatedly gone through \$1,000 during overnight trading, only to fall back when the US markets open. That indicates that the buyers are out east somewhere. I have written about this before: Gold is shifting from West to East – along with the balance of power.

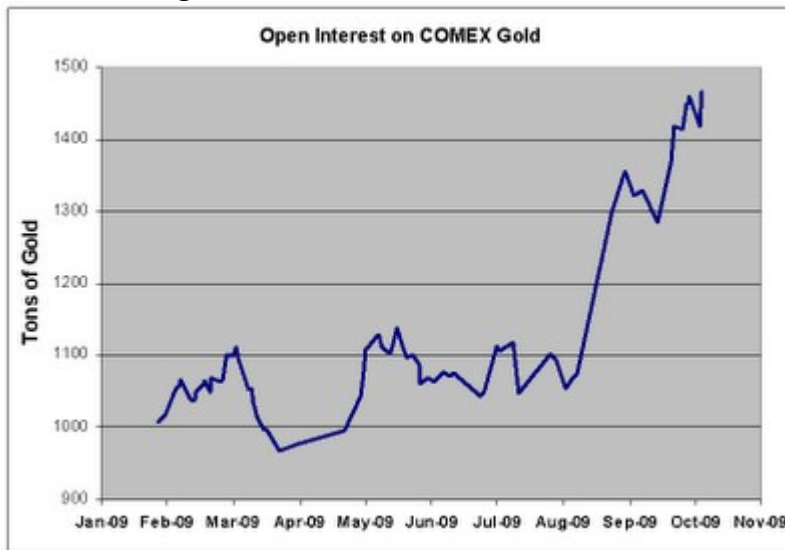
China is now [the driving force in the gold market](#) and can be counted on to buy whenever there is a price dip, putting a floor under any correction. So don't expect to ever see prices beneath \$900 again. With growing Chinese demand, Gold is never going back down.

Looking at [graphs of the price of gold](#), it is easy to see Chinese buying drive the market higher. For example, it was Asian buying which drove gold over \$1,000 on September 8.



Scary developments in gold

What is really scary about gold breaking the \$1000 barrier is that it happened in the face of a [flood short selling in US futures markets](#). So while gold was being driven up by Hong Kong buying, it has also been getting killed by unrelenting selling during COMEX hours. As can be seen in the chart below, the quantity of COMEX gold futures contracts has begun spiraling out of control since the end of August.



Open interest in gold futures is *EXPLODING*, yet gold prices have broken over \$1000 and are *STILL going up!* Demand for gold is reaching a level that cannot be stop as faith in the dollar disintegrates.

Investors emptying COMEX warehouses

In order to secure gold at the lowest possible price, US investors are turning to the complex, lengthy process of taking delivery of gold futures contracts. By buying gold contracts in deliverable months and wait for them to expire, sophisticated investors are [emptying COMEX warehouses](#). The incredible hassle of trying to pry gold out of Comex warehouses appeals to investors because no other place in the US offers a price equal to the Comex exchange. Nothing even comes close.

Guiding investors through the delivery process are gold and silver brokers like JB Slear who specialize in helping high net worth clients take delivery of gold and silver futures contracts. These advisors are necessary because, as investors are discovering, that there is [trouble at Comex warehouses](#):

- 1) *Delays and complications* in the delivery process have become increasingly commonplace. It is taking weeks and possibly even months, and sometimes dozen of inquiries, for investors to get the gold they already own out of the warehouse.
- 2) **More** restrictions are being applied to overseas buyers requesting delivery.
- 3) Some brokerages will not help with the delivery process or refuse to help even after the commissions are paid.
- 4) The cost in just about everything "Comex" is increasing
- 5) **Investors withdrawing their 100oz. bars from the Comex depositories are being given bars with incorrect serial numbers or weight.**

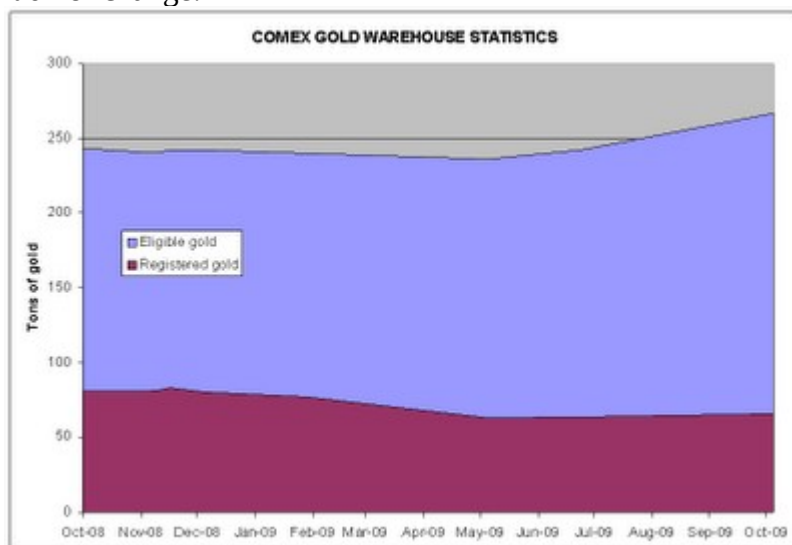
With the difficulties and irregularities in the COMEX delivery process, many, including gold brokers like JB Slear, have *doubts as to whether there is gold in inventory to match existing warehouse receipts.*

Like others involved in the gold market, **Slear believes that there are real shortages of precious metals that have yet to be exposed.** But he recognises the futures market as a last resort for people who can't buy metals at reasonable prices elsewhere: "If a buyer wants to buy a physical product and cannot find it locally, he or she can go to my firm's web address to transact that business. My business model is a last resort purchase arena for those who need to protect their personal wealth."

He says **there is anecdotal evidence that this activity is widespread enough to be affecting warehouse stocks as high net worth clients remove metal from warehouses.**

But, he [JB Slear] says that **the activity has yet to show up on Comex warehouse stock data:** "I find it interesting that **the Comex numbers don't show any movement at all as far as deliveries are concerned.** I have spoken to three of the warehouses and **each facility confirms the fact that the metals are being moved out, and in size.** One of my clients says that when she went to "will call" her purchase, that the "will call" staging area for deliveries was stacked high and busy. **Seems curious that the warehouse numbers reported through Comex, are not showing any reductions.** In the Comex defence though, I don't know how long it takes them to account for the movements. **I just keep my head down and focus on the job allotted me. That is to get the gold into my clients' hands as fast as possible.**

It is absurd that, as gold pours out of the Comex, warehouse stock data shows nothing. The chart below shows gold inventory levels at COMEX warehouse over the last year. Notice, above all, the **lack** of change.



Although warehouse facilities themselves confirm large gold outflows every month, the activity does not show up on COMEX warehouse stock data. Over the last year, total gold in COMEX warehouses **INCREASED 10% or 24 tons (868,000 oz).** See for yourself:

[COMEX Gold Stocks - October 30, 2008](#) (total=8.56 million oz)

[COMEX Gold Stocks - October 27, 2009](#) (total=9.43 million oz)

The sad part is that, even if Comex warehouse data is to be believed, there is only 66 tons of registered gold backing 1465 tons of gold promised for future delivery. So according to official data, there only enough gold to cover 4.5% of outstanding Comex gold futures contracts.

London Vaults also being emptied

Like Comex warehouses, London gold vaults are being emptied. Hong Kong is [pulling all its physical gold holdings from depositories in the UK](#) and moving their \$63 million worth of gold home to newly built vaults near the city's airport. Dubai is also planning to [withdraw its gold from London](#). Meanwhile, private investors and Swiss ETFs continue to move gold out of London.

On top of investor demand prying gold out London and COMEX vaults, [Germany and Switzerland are reportedly demanding the return of their custodial gold from the US](#). In the face of this onslaught of demand, the US/UK gold markets are crumbling

Widespread Abnormalities Across Gold Market

The strange activity in gold markets isn't limited to out of control open interest on gold futures or fictitious Comex warehouse data. Things are going wrong across the gold market.

1) Early this year, [The NYSE-Liffe futures exchange ran out of 1 kg bars of gold](#). Instead of receiving 1 kg bars as per mini-gold futures contracts, clearing members are now being allowed to hand out little slips of paper, called "warehouse depository receipts" (WDR), which gives the holder 1/3rd interest in a 100 ounce bar. Customers are not being allowed to take delivery, unless they can accumulate 3 WDRs. The NYSE effectively substituted the supply of 100 ounce bars for the supply of 1kg bars, which has run out. NYSE-Liffe mini-gold (YG) contract specifications were altered some time after December 31, 2008 to hide this default.

2) On March 19, [the Fed announced](#) its plan to purchase \$300 billion long-term Treasuries, \$750 billion (toxic) mortgage-backed securities, and \$100 billion (toxic) debt issued by Fannie and Freddie. This announcement was **INCREADIBLY BEARISH** for the dollar and bullish for gold. In the following two days, someone increased open interest in gold futures [by shorting 34 tons](#) (1,209,600 ounces) of gold. Who in their right mind would short gold following the fed's plan to go on a buying binge and load up its balance sheet with toxic debt?

3) Two major events happened in the gold market at the end of March this year:

A) **On March 31st, Deutsche Bank delivered 850,000 ounces of gold to Comex contract holders.**

B) **On March 31st, ECB announced it had "sold" 35.5 tons of gold (1,141,351 ounces).**

Circumstantial evidence and **common sense** suggest that the European Central Bank sold its gold to Deutsche Bank and [saved the bank and the Comex from default](#).

4) In the last three weeks, significant irregularities [significant irregularities have appeared](#) in the gold bar registry of GLD, with the length of the published GLD bar list going from 1,381 pages on September 25, to 208 pages on October 2, then back to 855 pages on October 14.

5) GFMS data on the volume of gold traded on the London market (about 90% of gold traded worldwide) [does not tally](#) with the estimated amount of gold bars which conform to "London Good Delivery" standard.

6) On October 29, 2008, the [TOCOM added](#) a 'physically backed commodity ETF' as a possible physical for EFP (Exchange of Futures for Physicals) transactions at the exchange. An exchange for physicals (EFP) transaction is when a client gives an IOU for a physical commodity to a broker and that broker opens a short position on the futures exchange in that commodity. Normally, Exchange for physicals is the legitimate process used by producers to sell futures against their future production. However, if the IOU portion of the EFP is not from a commodity producer (ie: borrowed a GLD Ishares), then you have a problem.]

In summary, New York and Tokyo commodity exchanges are now permitting their gold futures contracts to be settled not in real metal but in shares of gold exchange-traded funds (ETFs). This essentially allows those short gold (and the exchanges themselves, which guarantee futures contracts) the ability to transfer their obligations to third parties (commodity ETFs) that may not have the metal they claim to have.

7) Half a ton of gold [has disappeared](#) from the Royal Canadian Mint. An independent audit released on July 3rd found no accounting, bookkeeping, or other internal errors could account for about 17,500 troy ounces of gold missing from the mints inventory. [Fearing a "run" on its gold](#), Royal Canadian Mint is reassuring customers their deposits are fully accounted for and in secure vaults. A RCMP investigation into the \$15.3 million missing gold is "ongoing." (If half a ton of gold could disappear from one of the most secure buildings in Canada, then Isn't it about time for [US gold reserves to be audited?](#))

8) Rob Kirby is reporting some VERY SERIOUS developments in the gold market, which, although I have no way to verify them, seem creditable in light of everything else that I KNOW is going):

A) During the week of Oct. 5, some large allocated physical transactions that were settled in London [under VERY strange circumstances](#). Banks like JPMorgan and Deutsche Bank (who sold endless amounts of gold futures at prices of 950 to 1025) and then tried to make "side deals" with the folks they sold the futures to – offering them spot + 25 % (around 1,275 per ounce) to settle in fiat – after their counter parties demanded substantial tonnage of physical gold bullion.

B) A number of large interests have demanded audits of gold stored in London.

C) In an Asian depository, they've found "Good Delivery" bricks that had been gutted and filled with tungsten.

9) US-based clearing house CME Group Inc. is [allowing physical gold to be used as collateral](#) for margin requirements on all exchange products. This new CME policy is an act of desperation. The decision to "allow physical gold to be used as collateral for margin requirements on all exchange products", against a backdrop of record prices and widespread abnormalities in gold markets, screams that something is wrong. The policy would never have been proposed unless JPMorgan really, really needed gold.

10) Statistics from United States Geological Survey show that the united states has [exported 5000 metric tons of "Gold compounds"](#) in last two years, and the US Census Bureau has assigned an astronomically high value to these exports. Until someone explains to me what these "gold compounds" are, I am going to assume that they were half the US gold reserves leaving the country.

The gold market is an accident waiting to happen

Basically, the gold market operates on a fractional reserve basis. On average there are several claims of ownership on each gold bar conforming to London Good Delivery (LGD) standard on the "pool" of gold which acts as liquidity for the massive OTC gold trade based in London. Similarly, there are several claims of ownership on the gold bars in Comex warehouses. If a sufficient number of market participants become concerned about this (which is happening) and there is a stampede to take delivery of physical bullion, the entire gold market will come crashing down, taking most of the global financial system with it. Market failure isn't a risk, it is a certainty. The unregulated gold market is an accident waiting to happen.