



## HOW MUCH GOLD HAS BEEN SOLD THAT DOESN'T EXIST?

**Adrian Douglas**

On October 9 I published an [article](#) that postulated that the gold market is a Ponzi scheme because it sells gold that doesn't exist by implementation of the principles of fractional reserve banking. Since writing that article further information has come to light which supports this claim and allows an estimate of how much gold has been sold that doesn't exist if the owners of the gold ask for it. In other words there are several owners for each ounce of physical gold.

By complete coincidence Paul Mylchreest of The Thunder Road Report has just written an in-depth study into the daily trading volumes of gold on the London OTC (over-the-counter) market which you can link to [here](#). The London OTC market is where most of the physical gold in the world is traded. This market is a wholesale market where trades are only conducted between the bullion trading houses on behalf of their clients. About 95% of the trading is by way of gold that is held in unallocated bullion accounts. The unique characteristic of gold is that about 50% (80,000 t) of the world above ground gold stocks are held as a store of wealth (investment). The other 50% exists as jewelry. When gold is bought as a store of wealth it can perform that function for you where ever it is in the world. Given this unique characteristic many large investors in bullion prefer to leave their gold with the bullion dealer from whom they bought it so that it can be stored in their vault and easily re-sold. This is identical to the situation with stocks where most stock certificates are held by the brokerage house not by the individual.

The fact that people are buying and selling gold without ever taking delivery means that there is the opportunity for the bullion houses to sell gold that doesn't exist. Now the bullion houses probably don't view this as illegal or dishonest because they will operate a fractional reserve type system just as the banks do with fiat currency and make sure they have enough gold on hand for what would be the maximum estimated volume of gold that could be called for delivery. After all trading is done with unallocated gold so how much more unallocated can it get if it doesn't exist at all!?

This is what caused bank runs in the days of a gold standard. People would deposit gold in a bank and receive bank notes (dollar bills) in exchange. At anytime the depositor could return and hand over his bank notes and receive the same quantity of gold that he originally deposited from the bank. The banks realized that under normal circumstances a maximum of about 10% of the gold deposited could be requested.

The banks saw an opportunity. They could issue up to ten times as many bank notes in loans as gold in the bank and earn interest on the bank notes. The system worked until the time when there was difficulty meeting withdrawals. Then word would quickly spread that the bank was insolvent and as holders of the bank notes rushed to the bank to redeem them for gold the bank would admit it had insufficient gold and would declare bankruptcy. The origin of the word “bankruptcy” is from the Latin words “bancus” and “ruptus” which means literally the bank is broken. In history banks have gone bust frequently enough to have earned themselves the honor of ownership of the word to describe the phenomenon! Isn't that ironic when banks are meant to be a safe store for money!

This basic scam is at the center of modern gold market manipulation. Paper substitutes for gold are sold instead of real gold through derivatives, futures, pooled accounts, ETF's, gold certificates etc. I estimate that each actual physical ounce of gold has multiple ownership claims to it. For the scam to be sustained there must always be plentiful physical gold for those who want it. The market is, in effect, a giant inverted pyramid with a huge paper gold market being supported above a small amount of physical gold at the tip of the inverted pyramid. The scam can continue until there are indications of a shortage of physical gold. If all the claimants of each ounce of real gold demand their gold then there is the potential for a squeeze like has never been seen before in history.

To lend support to the idea that all the gold in the world has been sold several times over I cite the case of Morgan Stanley who were sued in 2005 for selling non-existent precious metals to their customers. They even had the audacity to charge storage fees! They settled the class action suit out of court but no criminal charges were ever filed against them. If Morgan Stanley was doing this you can bet that it is the tip of the iceberg.

Paul Mylchreest has done fabulously detailed research into data that exists on the daily trading of gold on the London OTC market. He concludes that 2,134 tonnes of gold are traded each and every day! That is a real shocking number because this is 346 times larger than all the gold that is mined in the world each day! But this on its own is not sufficient evidence to indicate that the market is fraudulent. For example, if I have a 1 oz gold coin and I have 100 friends I could sell the coin to a friend and then he could immediately sell it back to me or sell it to one of my other friends who could sell it back to me. If I were to transact with

all my friends in the same day in this way I could have turned over a volume of 100ozs in trading transactions but no fraud would have occurred because the last friend I traded with owns the 1 oz coin but it went through 100 different hands before it got to him. There are no multiple ownership claims to the coin because the trades were sequential not simultaneous. If, however, I were to sell 1 oz of gold to all my friends and promise I would keep the gold for them, the trading for the day would be 100 ozs but now fraud has been committed because I have a liability 100 ozs of gold but I only have 1 oz! But if they never ask for the gold and I can pay them cash when they want to sell their gold then there is a good chance my friends would be none the wiser...until the day at least two friends insist on receiving the physical 1 oz coins they each supposedly own!

The daily gold trading in London is simply humongous. We talk of the gold market being a tiny market. It is anything but. It has a daily turnover of 70 Billion dollars. To put this in perspective the world consumes 86 million barrels of oil each day. The total cost of the global daily oil consumption is a mere 6 Billion dollars!

But as discussed above, the daily volume traded does not in and of itself prove that a fraudulent fractional reserve operation is being conducted. Mylchreest did some more work using GFMS statistics to determine the maximum quantity of gold stock the OTC market could be holding with which it can back the huge daily trade volume. The gold that is traded has to be in the form of London Good Delivery (LGD) bars which are 400 ozs bars. Mylchreest estimates that there can only be about 15,000 tonnes of such bars in the world. Let us assume that the London OTC market holds them all. We will show that by comparison with the trading of other unallocated gold products 15,000 tonnes is nowhere near enough gold stock for the gold not to have more than one ownership claim to each ounce.

The purpose of buying investment gold is for it to store wealth. This necessarily implies that it is held for a long period of time. If gold is bought and traded quickly it would destroy wealth not store it because there would be a large loss due to transactional fees. The figures we have so far suggest that the entire stock of gold of the London Gold market could be turned over every 7 days ( $15,000/2,134 = 7$ ). That would hardly be characteristic of a market that is supposed to be selling a "buy-and-hold" type product. For the purposes of illustration, in a town of 15,000 houses would you expect 2,134 houses to be sold each day? Or that each house on average would have 52 different owners during the year?

Let's compare how much of the inventory of the precious metal ETF's are traded each day to get a good idea about how frequently investors trade something they have bought as a store of wealth. The most liquid and highly traded ETF is GLD. It has 325 million shares outstanding and the fund trades on average 11.9 million shares each day. This means it trades 1 share each day for each 30 shares that are outstanding. Central Fund of Canada trades 1 share for each 140 shares

outstanding, while the Gold Trust Unit trades one share for each 300 shares outstanding.

The GLD ETF is a way of buying, holding, or selling unallocated gold. One would expect the investors' behavior in this ETF would be similar to those trading the unallocated accounts on the OTC. If the investor trading mentality on the London OTC is similar then 2,134 t should be 1/30<sup>th</sup> of the gold stock held by the OTC. This equates to 64,000 t of gold. But Mylchreest estimates that the OTC can hold no more than 15,000 t because that is the entire global stock of LGD bars. If we use the CEF example the stock would have to be 298,000t or the GTU example it would have to be 640,000t!

Probably the GLD comparison is the most relevant as it claims to hold 1100 t of gold which is comparable to the maximum 15,000 t that could be held by the OTC participants. However, the OTC is restricted to wholesale traders and has a minimum trade limit of 1000 ozs. In GLD the minimum trade is 0.1 ozs and is open to everyone. Considering these limitations it is likely that OTC participants would turn over a lot less than 1/30<sup>th</sup> of the inventory in a day. However, even taking the GLD estimate the OTC participants should be holding 64,000 t when according to what can be deduced from GFMS statistics they can only be holding 15,000 t. This means that each ounce has at least 4 owners! I think this is probably very conservative because the GLD vehicle is set up to be easily traded and in units as small as 0.1 oz. I would guesstimate that it is more likely to be as high as 10 or even 20 owners to every ounce, particularly when the banking world has used 5-10% reserve ratio with fiat money for a long time and bankers are creatures of habit. This would imply that the liability for unallocated gold that has been sold is probably closer to 150,000t (taking the more conservative 10% figure) but the liability is backed by a totally inadequate maximum of only 15,000t of physical gold. It is, therefore, probable that anywhere between 45,000t to 135,000t of unallocated gold has been sold that does not exist. This is around 50% to 170% of the entire existing investment gold stock that has taken 6000 years to mine and accumulate!

We are hearing of more and more cases of gold investors wanting to take physical delivery or have allocated gold. In my recent article I said:

*“A couple of months ago Greenlight Capital, the large hedge fund, switched \$500 million of investment in GLD to physical gold bullion. ....Apparently Germany has requested that its sovereign gold held by the NY Federal Reserve Bank be returned to Germany. Hong Kong has requested the same of the Bank of England that stores its sovereign gold. Robert Fisk, a respected journalist for the UK's Independent newspaper, reported this week that the Arab oil producing states, Japan, Russia and China have been holding secret talks to replace the dollar as the international reserve currency and as an accounting unit for trade. He reports that the basket of currencies they propose instead of the dollar would include gold! If gold is going to regain its monetary role then you can understand*

*why those in the know want actual physical bullion. There are some very real and significant signs that a run on the bank of the Gold Cartel for physical gold is commencing”*

Talking of runs on the bank, Rob Kirby of KirbyAnalytics and GATA consultant did some brilliant [sleuthing work](#). His sources have told him that there was panic in the London gold market around September 30<sup>th</sup>, 2009 as participants in the market wanted to take delivery of their purchased gold and refused generous cash settlements that were offered instead. Central banks had to come to the rescue to provide the gold via leasing. Apparently, even the Central Banks could not provide bars that met LGD specs which indicates a very acute shortage of physical gold is developing and that perhaps already many OTC clients have drained a large proportion of the 15,000 t of gold stock from the London OTC market. This supports what I have been discussing above. Paul Walker, CEO of GFMS, recently said that gold was going up because of some large lumpy transactions in a market with a degree of illiquidity! If the OTC was only selling gold that the participants own there could never be a lack of liquidity. The panic that occurred at the end of September confirms there is a chronic lack of liquidity. This necessarily implies that there is multiple ownership of the same ounce of gold and it is, therefore, fraudulent. Leasing of gold from Central banks only provides temporary liquidity because they want it returned at some later date, and it looks as if the bullion bankers may have dipped into that well one too many times already!

The gold market is in a precarious position. Just like in the days of the gold standard it only required one customer not having his deposit returned to bring down the bank because a domino effect is initiated that results in all depositors asking for their deposits to be returned. If my estimates are correct that somewhere between 64,000 and 150,000 tonnes of gold have been sold against a reserve of only 15,000t. But how much of this 15,000t remains? The panic at the end of September suggests liquidity is very tight in which case only a small percentage of investors asking for their gold to be delivered or placed in an allocated account will blow up the gold market and expose the scam (a scam that has been repeated time and time again throughout history with some variations on the basic theme and has always ended in crisis and huge losses. Why should this time be any different?)

If you “think” you own gold you should take a few more steps to make sure that you do actually own gold. If you have unallocated gold in some sort of pool account that does not have a satisfactory audit or you own shares in an ETF that does not have a reliable audit then take action. Take delivery of gold or move your investment to reliable and audited allocated storage.

If you do nothing about it and when the music stops you are left with just a piece of paper that says you own gold but no one is able to give it to you then perhaps you will be able to take comfort in the fact that you dismissed the German Government, the Hong Kong Government, Greenlight Capital and many others

as just a bunch of nuts who don't know as much as you about counterparty risk in the gold market! But the "nuts" who are realizing that there are multiple ownership claims to each ounce of gold will at least have their gold if they ask for it first!

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