DAILY RECKONING

Central Bank Gold

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Free Research Report:

The Real Reason the World's Central Banks Are Stockpiling Gold

"I don't see any inconsistency with our policy and maintaining a strong dollar… The Federal Reserve's price stability record is excellent, and we are fully committed to maintaining it."

So said Federal Reserve Chairman Ben Bernanke last October, expressing his confidence that the Fed, of course, had "the right tools" at its disposal.

Markets seem to believe him: The Dow Jones is nearing its all-time high; the S&P 500 just hit a five-year high; gold prices have fallen dramatically, inflation is low and unemployment seems to be shrinking.

"This year is setting up to be the year in which the secular bull run in gold finally ends" declared Forbes in January. "So long gold $2,000. We hardly knew ye."

You might be tempted to think that the global economy is recovering, the dollar strengthening and gold will finally sink into obscurity.

Think again.

Central bankers like Ben S. Bernanke may tell you that banks hold gold bullion only for sake of "tradition," but gold traders know otherwise — gold is real money, and despite what bankers, economists and mainstream investors have been saying, they are terrified of a **coming currency crisis**.

To shore up their reserves in anticipation of a major global credit default, central bankers are doing the only thing that makes sense — **stockpiling gold.**

The mainstream media have largely ignored these moves and downplayed their significance, but we know from experience it is important to consider the reasons behind these actions, and the message being sent to investors by central banks around the globe is **gold is money.**

Our research is going to show you a glimpse into what has been happening behind the scenes at some of the world's largest central banks — what it might mean for the price of gold… and **how you can take advantage of low prices before gold reaches again for $2,000 and beyond.**

Germany

In January 2013, Germany made big news by announcing its plan to bring home part of its massive gold reserves. By retrieving 300 tons from New York and all 374 tons from Paris, 19% of its holdings — $36 billion worth — will be repatriated. By 2020,

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the Deutsche Bundesbank expects to have 50% of its gold reserves stored in its Frankfurt vaults.

The reason given by the German central bank for its recently announced repatriation plan was to "build trust and confidence domestically, and the ability to exchange gold for foreign currencies at gold trading centers abroad within a short space of time."

The Bundesbank has made it clear that this is not to be taken as a sign that it will be selling gold. **Quite the opposite, as it also stated that this move is a "pre-emptive" measure "in case of a currency crisis."**

If global markets are improving, debt is no big deal and fiat money is sound — why is the Bundesbank worried enough to spend millions of dollars moving 300 tons of gold across the Atlantic for the first time in over 50 years in a highly risky series of transport operations?

Venezuela

You'll likely recall Hugo Chávez's repatriation of Venezuelan gold in late 2011 — a decision that was widely believed to be motivated by fears of U.S. sanctions and frozen assets.

Chávez, however, said the move was to "safeguard against volatility in financial markets."

Admittedly, Chávez's decision did not hold the same weight as Germany's in the eyes of the world. Germany is an ally of the U.S., after all. However, having repatriated his gold just months before Europe's debt crisis took hold, it's hard to dismiss the foresight demonstrated by the 15th-largest gold holder in the world.

Russia

Russia, with the eighth-largest holding of gold in the world — almost 938 tonnes (over $50 billion) — has been increasing its gold holdings hand over fist in recent years. In 2012, its gold reserves increased a hair shy of 55 tonnes, more than 6%. **The reason given, according to Reuters, is "to diversify its foreign reserves away from paper assets it views as risky."**

One Russian lawmaker, Evgeny Fedorov, laid out the Russian government's strategy:

"The more gold a country has, the more sovereignty it will have if there's a cataclysm with the dollar, the euro, the pound or any other reserve currency," he said in a phone interview with Bloomberg.

Furthermore, the gold purchases here are only the officially reported ones: **A large percentage of central bank gold purchases go undisclosed**. They are completed through third-party contracting companies with the utmost discretion.

"The United States Federal Reserve and the European Union… are in the process of a de facto devaluation of their respective currencies, by printing tremendous amounts of dollars and euros…" — Gold Initiative, Parliament of Switzerland

Switzerland

In 2011, an alarm was raised as many realized that more than half of the Swiss national gold had been sold off. This gave rise to the "Gold Initiative: A Swiss Initiative to Secure the Swiss National Bank's Gold Reserves." Launched by four members of the Swiss parliament, the goal of the initiative is clearly identified in the name: to keep gold reserves secure through three requirements:

1. The gold of the Swiss National Bank must be stored physically in Switzerland.
2. The Swiss National Bank does not have the right to sell its gold reserves.
3. The Swiss National Bank must hold at least 20% of its total assets in gold.

Two of the main reasons given for desiring to secure these reserves are: **"The United States Federal Reserve and the European Union (with the European Central Bank ECB) are in the process of a de facto devaluation of their respective currencies, by printing tremendous amounts of dollars and euros"**; and "These actions strongly affect the Swiss National Bank, as the Swiss franc runs the risk of being devaluated as well." As is stated clearly, "The greater the risk, the more important it is to maintain a sufficient gold stockpile!"

The Netherlands

Of the Netherlands' 612.5 tonnes of gold, only about 11% is in Dutch vaults. Over half is in New York, with the rest divided between London and Ottawa. Recently, the Dutch Christian Democratic Appeal Party has made an official appeal to repatriate the Netherlands' gold reserves.

Netherlands Info Services reports: "More and more citizens, politicians and economists in Europe are questioning **whether the foreign gold reserves, which their country possesses on paper, are still in fact physically there."**

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They're not being paranoid: Central banks don't actually have to have the gold in their vaults in order to claim it on paper, and Western central banks are notoriously secretive about their gold stashes.

There is other evidence for the possibility that central banks are loaning off gold reserves: According to Sprott Global Resource Investments, despite dramatically increasing demand for gold over the last decade that mining and jewelry

recycling haven't been able to keep up with, the supply seems to be rising concomitantly with demand. Central banks seem the most likely culprit, since their gold is untraceable.

What does this mean?

It means gold repatriation currently under way may reveal that central banks haven't been so honest about their gold holdings, which could lead to serious scrutiny of foreign gold holdings — or even an unprecedented "gold run" on central banks. In the event this happens, the gold price could head for the moon.

"No asset is safe now. The only choice to hedge risks is to hold hard currency — gold." — Zhang Jianhua, People's Bank of China

China

While the World Gold Council reports China as owning just over 1,054 tonnes of gold, it's a well-known fact that the Asian powerhouse is very secretive about its true holdings until it sees an advantage in reporting.

Even then, speculation abounds as to the verity of its claims. Some have estimated that, in light of the 1,054 tons being reported in 2009, by the end of 2013, China may hold as much as 4,000 tons of the yellow metal.

Even if this is true, it would still represent only approximately 8% of its total reserves. **However, the gold market could react quite strongly if China announced reserves anywhere near these levels.**

As the world's largest gold producer for the past six years, China is perfectly capable of building reserves under the radar. Furthermore, due to its secrecy regarding its holdings, don't hold your breath waiting to find out how much gold it's holding. We expect that China, like Russia and many other countries, will continue to dump U.S. dollars while acquiring gold.

So why is China buying so much gold? The People's Bank of China's Zhang Jianhua said in December 2011: "No asset is safe now. The only choice to hedge risk is to hold hard currency — gold."

You, the Investor

As investors, we should take note. After a couple decades of shunning gold as a useless relic, banks are refixing their sights on the yellow metal, for many reasons. Central to these is the reality that gold represents the world's true money.

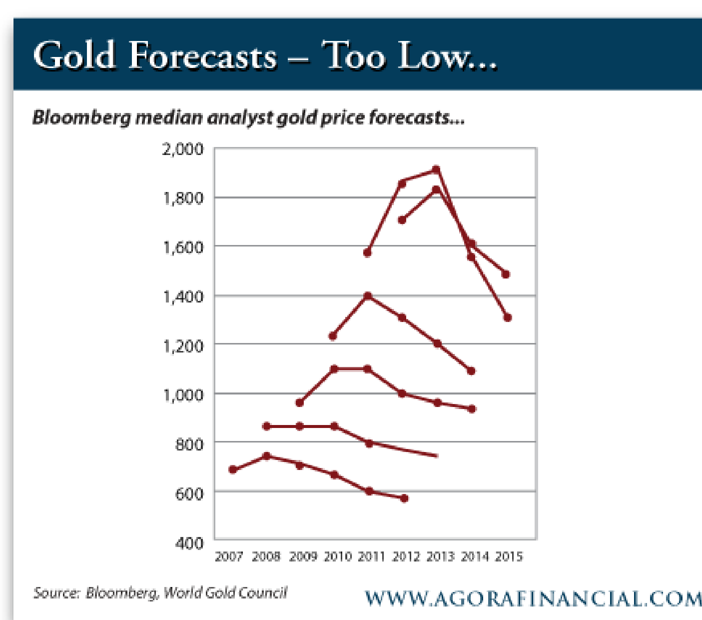
Whether we're attempting to diversify our portfolios or hedge against inflationary fiscal policy, true money is one of the few tangible monetary investments backed up by its own historic value — 6,000 years' worth.

Other central banks not mentioned in this research are aggressively increasing their gold reserves, such as Kazakhstan and Turkey; still others, such as Mexico, are auditing their holdings in Western central banks.

Regardless of the daily turmoil in the gold price, the long term buy-and-hold value of gold remains unchanged, and there's no better evidence than the actions of the world's central banks.

You might be tempted to think the gold boom has run its course with so many banks and media outlets adjusting their price forecasts downward in recent weeks.

Mainstream analysts, however, have been wrong on their gold forecasts for years. Bloomberg data show that most analysts have consistently underestimated gold's potential:



The way to read this chart is to start on the far left. That first line, the lowest line, is a plot of the 2007 forecasts. You can see analysts projected a gold price of less than $600 an ounce by 2012.

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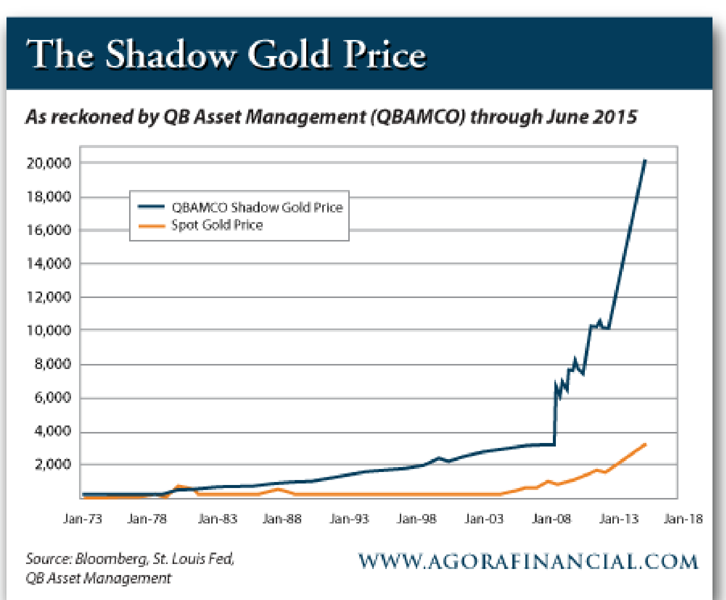
The next line up, which begins in 2008, is a plot of the 2008 predictions. You can see the predicted gold price was under $800 an ounce. In each set of predictions, analysts not only forecast gold prices too low, but they forecast gold prices to decline a few years out.

Devaluation of fiat currencies highlights the importance of maintaining a sufficient gold stockpile. Central banks are embracing policies of anywhere from 5–90% gold reserves. Carefully consider their reasons and whether you are sufficiently diversified.

So where will gold go?

We can make some inferences using the Shadow Gold Price (SGP) calculated by QB Asset Management. The SGP uses the Bretton Woods calculation for determining the exchange rate linking gold to the U.S. dollar. The calculation is base money divided by U.S. official gold holdings. This is useful because it tells us how many dollars are out there chasing ounces of gold, which can give us some idea of where the price in dollars might go in the long run.

Here is QB's latest chart. It includes projections of the base money supply through June 2015, assuming the Fed prints $85 billion per month. The SGP soars to $20,000 per ounce:

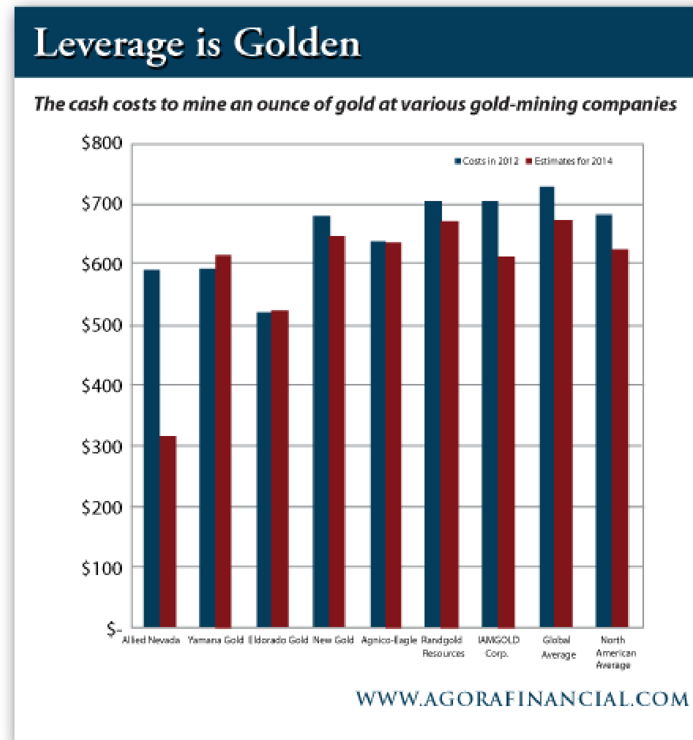


If the ratio between the Shadow Gold Price and actual gold prices stays constant, gold could be **$3,400 per ounce by 2015!**

If gold rallies anywhere close to $3,400 by 2015 (QB Asset Management's scenario), **quality gold mining stocks could rally by several hundred percent.**

You could consider adding some of the midsized gold miners in the table below. The estimates are from RBC Capital Markets.

Investors will pay a premium for gold miners with consistent execution and low, stable cash costs. The companies in the table below have these qualities. Stable cash costs should translate into good stock price performance.



The companies are: Allied Nevada, Yamana Gold, Eldorado Gold, New Gold, Agnico-Eagle, Randgold Resources and IAMGOLD Corp.

An Old Relationship Renewed

It's quite evident that the relationship between the world's central banks and gold has been changing in recent years. Just 15 years ago, many were selling gold reserves at rock-bottom prices, seeing no real value in maintaining such vast quantities.

Today these same countries are facing public outcry as the citizenry realizes, albeit too late, that the real sovereign wealth of their nation has been squandered by myopic monetary policies.

It seems unlikely that the real trend — away from trust in fiat dollars, even among the central banks that print them — is going to change.

Regards,

Greg Kadajski
Managing Editor
The Daily Reckoning

P.S. **I can't believe they're trying to do this**

Have you seen what the Chinese have begun to do with their gold?

It's absolutely astonishing…

Steady yourself, then **click here** to see it.