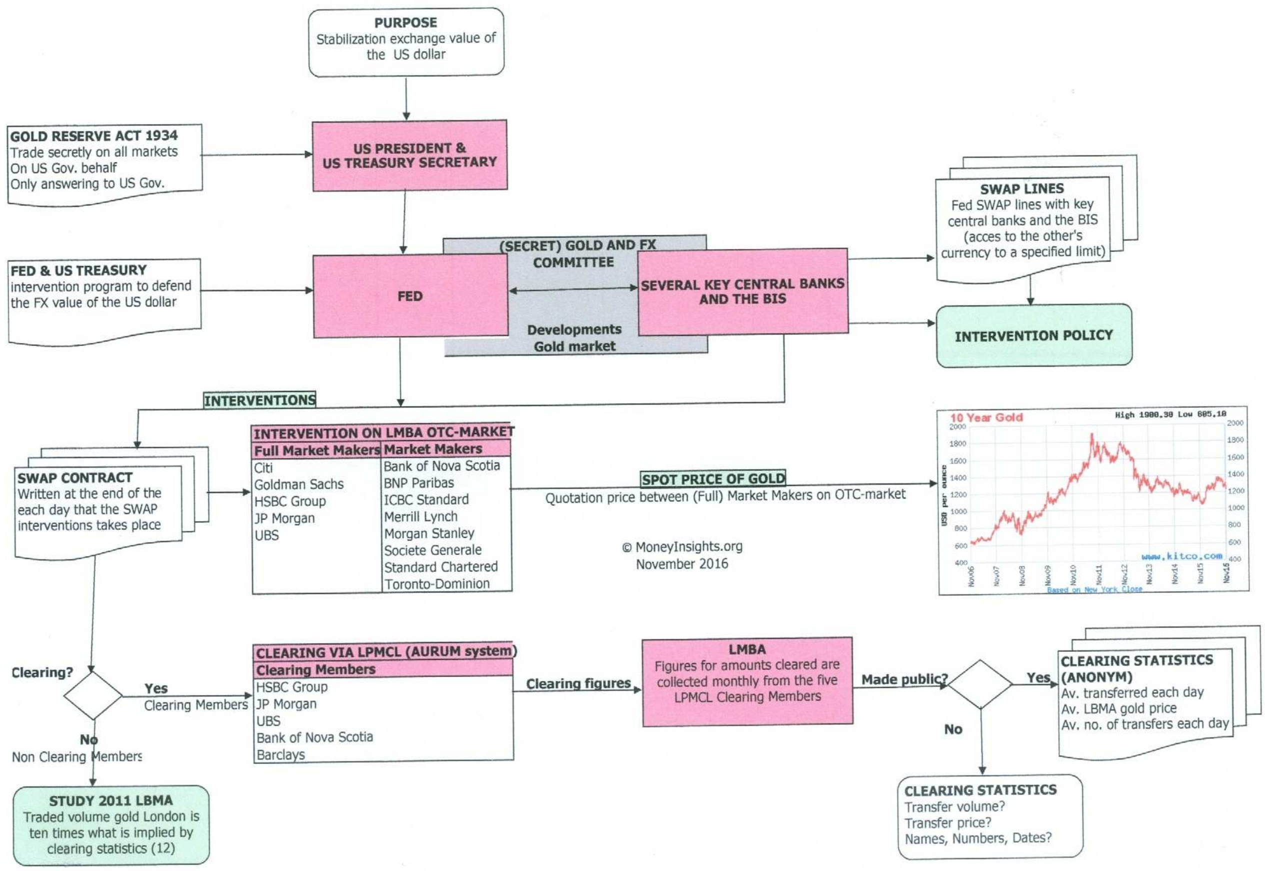
Gold Price Intervention Circuit Diagram and Determinants Intervention Policy

1. Introduction

This is an article about abuses in the gold market. It is meant to be for readers, who are well informed and interested in the gold market and monetary items, such as student (central) bankers, politicians, financial analists, supervisors, etc.

Based upon study we (re)constructed the Gold Price Intervention Circuit Diagram. The purpose for the (secret) interventions is the stabilization of the exchange value of the US dollar. There are many actors involved by the interventions vary from politicians, central bankers, institutions like the BIS, IMF and LMBA, Market Makers on the OTC-market (commercial banks), and Clearing Members LPMCL. We call an intervention secret if it has not been reported to market participants at the latest on the day the intervention was carried out by the one or two involved central banks, or not being reported at all (13).
Furthermore we (re)constructed some determinants of the (secret) Intervention Policy on the price of gold by central banks.

2. Gold Price Intervention Circuit Diagram



3. A short explanation on this Intervention Circuit Diagram

About the Gold Reserve Act of 1934 (1)

…Authorization to deal in gold and foreign exchange with approval of the US President…

The Gold Reserve Act of 1934 established a fund (so-called Exchange Stabilization Fund) to be operated by the Secretary of the Treasury, with the approval of the President. Section 10 of the Act provided that "FOR THE PURPOSE OF STABILIZATION THE EXCHANGE VALUE OF THE DOLLAR, the Secretary of the Treasury, with the approval of the President, directly or through such agencies as he may designate, is authorized, for the account of the fund established in this section, to deal in gold and foreign exchange and such other instruments of credit and securities as he may deem necessary to carry out the purpose of this section."

As per 30 September, 2015 the total assets of the fund amount to USD billion 93.

About Bretton Woods system

The Bretton Woods Agreement is the landmark system for monetary and exchange rate management established in 1944. The agreement pegged the exchange rates of nations to the value of the US dollar, witch in turn was pegged to the price of gold. An overvaluation of the US dollar led to concerns over the exchange rates and tie to the price of gold. In 1971 president Nixon found it necessary to suspend the dollar's convertibility into gold and several major currencies were allowed to float against the dollar (era of floating rates).

In the 1960s, the Bank for International Settlements (BIS) was at the center of central bank efforts to keep the price of gold in the free market trading near its official price in the Bretton Woods system (so called Gold Pool).

About SWAP Lines

…SWAP network…Gold is a premier currency…

On 1 November, 1978, the Federal Reserve and the US Treasury announced a new and expanded program to defend the foreign exchange value of the dollar. A major aspect of the expanded intervention capability was a increase in the size of Federal Reserve's SWAP lines with several key central banks (so called the "SWAP network"), thereby allowing greater foreign exchange borrowings for purposes of interventions.

The SWAP network is a set of short-term reciprocal currency agreements the Federal Reserve maintains with the 14 (1978) foreign central banks and the Bank of International Settlements (BIS). Each agreement allows the Federal Reserve and his partner bank short-term access to the other's currency up to a specified limit. A SWAP contract is written at the end of each day that the Federal Reserve SWAP intervention takes place.

Central banks try to make their intervention seem as random as possible to avoid traders forecasting it and capitalizing on it (2).

Table. Federal Reserve Swap Lines
(US$ million)

	30-Sep-96	30-Jun-04	04-Nov-08
European Central Bank	...	50,000	110,000
Bank of Japan	5,000	0	60,000
Bank of England	3,000	30,000	40,000
Bank of Korea	0	0	30,000
Bank of Mexico	3,000	3,000	30,000
Central Bank of Brazil	0	0	30,000
Monetary Authority of Singapore	0	0	30,000
Swiss National Bank	4,000	0	27,000
Reserve Bank of New Zealand	0	0	15,000
Bank of Australia	0	0	10,000
Bank of Canada	2,000	10,000	10,000
Bank of Sweden	300	0	10,000
Bank of Norway	250	0	5,000
National Bank of Denmark	250	0	5,000
Austrian National Bank	250	...	...
Bank of France	2,000	...	...
Bank of Italy	3,000	...	...
Deutsche Bundesbank	6,000	...	...
National Bank of Belgium	1,000	0	...
Netherlands Bank	500	...	...
Total	30,550	93,000	412,000

Source: U.S. Federal Reserve. Reciprocal Currency Arrangements.

In 2008 the FED extended the SWAP lines due to their concerns about the global dollar liquidity.

Don't forget gold is a currency:
The BIS stated in its 2013 annual report that "gold is to be dealt with as a foreign exchange position rather than a commodity because its volatility is more in line with foreign currencies, and banks manage it in a similar manner to foreign currencies".

Ex-Fed-Chief Alan Greenspan told The Council of Foreign Relations on 29 October, 2014 to remember what gold is. Gold is a currency. It is still, by all evidence, a premier currency.

<u>About the SWAP network in practice</u>

...Secret currency interventions by central banks...

According to the publication of Februari, 1978 of the Federal Reserve Bank of St. Louis were the gold reserves actually not used for interventions, due to the current practices as evidenced by SWAPS (3).

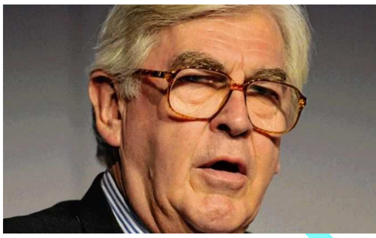
The Riskbank is open about the interventions. In October, 2016 is mentioned on their site:
The Riskbank is Sweden's central bank and responsible for monetary policy with the objective to maintain price stability. The Riskbank is joint shareholder of the BIS. According to the Riskbank is their gold reserve justified, to a large degree, by the fact that the value of gold does not normally follow the same pattern as the value of the foreign currency reserve. The gold can be used to fund emergency liquidity assistance or foreign exchange interventions, among other things.
Further the Riskbank has concluded an agreement with a number of other central banks, the Central Bank Gold Agreement (CBGA), witch places a limit on the amount of gold the may sell each year. The aim of the agreement is to limit the central bank's sales of gold in order to avoid undesirable effects on the gold price.

A confidential IMF report from March, 1999 about the reporting template for central banks advices western central banks to conceal their gold loans and SWAPS because information about them is "highly market-sensitive" and accountability about them would "hinder secret currency" interventions by central banks, in view of the limited number of participants in such transactions (4).

The FED, the central banks and the BIS formed the (secret) Gold and Foreign Exchange Committee. In restricted-controlled notes on the discussion of the gold market at the meeting of the secret Gold and Foreign Exchange Committee of the G-10 Governors at the BIS on 7 April, 1997 Terry Smeeton, head of foreign exchange and gold at the Bank of England said that in May 1996 the SWAP deals accounted for 75 percent on the trading volume in the London market (5).

Participants Gold and Foreign Exchange Committee on 7 April, 1997

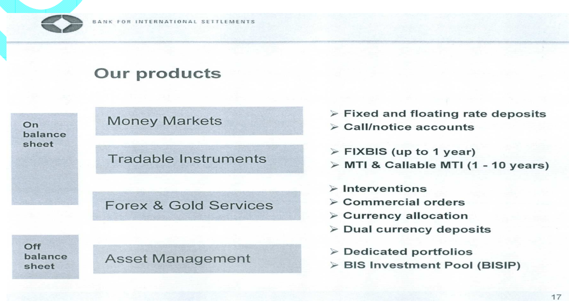
Name	Country	Central Bank	Jobtitle
Dino Kos	United States	Federal Reserve System of NY	Head Fixed Income and Foreign Exchange
Ian Plenderleith	United Kingdom	Bank of England	Member Monetary Policy Committee
Terry R Smeeton	United Kingdom	Bank of England	Head of Foreign Exchange Division
Bruno Gehrig	Switzerland	Swiss National Bank	Board Member, Head SNB Monetary Operations
GM Gill	BIS	Bank for International Settlements	Head of Banking Department
Peter R Fisher	United States	Federal Reserve System of NY	Executive Vice President, Manager Open Markt Account, responsible FOMC
William R White	BIS	Bank for International Settlements	Economic Advisor and Head of the Monetary and Economic Department
Edwin M Truman	United States	Federal Reserve System	Director Division of International Finance, Staff economist FOMC
Alf Mainert	Germany	Deutsche Bundesbank	Bundesbankdirektor
Don Stephenson	Canada	Bank of Canada	Senior Advisor, Canadian Foreign Ecchange Committee
Jean-Pierre Patat	France	Banque de France	Director-General of Economic Studies and International Relations
Johan Heikensten	Sweden	Sveriges Riksbank	Deputy Governor of Sveriges Riskbank, responsibel for Monetary Policy
Fabrizio Saccomanni	Italy	Bank of Italy	Deputy Governor
Herman Bussers	Belgium	National Bank of Belgium	Departmentsadvisor, Foreign Department
Jos Heuvelman	Netherlands	De Nederlandsche Bank	Director Financial Markets
Akira Nagashima	Japan	Bank of Japan	Deputy Governor for International Relations



Ian Plenderleith,
Bank of England,
Chairman Gold and Foreign Exchange Committee

William R. White, Head of Monetary and Economic Department at the BIS, held an outspoken speech at the fourth BIS Annual Conference, on 27 – 29 June 2005, while celebrating the 75 years existing of the BIS (1930 – 2000). Mr White mentioned the five intermediate objectives of central bank cooperation. The fifth objective was the joint effort of central banks to influence the price of gold and foreign exchange (11).

On 10 February, 2010 Michel Beine (University of Luxembourg) reported that the bulk of central banks interventions is located between 7.00 and 15.00 EST which suggests that the FED intervened using their network of US commercial banks. But choosing the timing might be a strategic issue: The Bank of Japan intervened outside Japanese time tot conceal interventions.



Presentation BIS about their products,
items Forex & Gold Services, Interventions

In its 2010 annual report, the BIS said that “gold, which the bank held in connection with gold SWAP operations, under which the bank exchanges currencies for physical gold, stands at 8,160.1 million SDR, equivalent to 346 tonnes this year.”

Here are some shocking results from a survey held by Christopher J. Neely (senior economist with the FED of St. Louis) among 22 monetary authorities in June 2001.

FEDERAL RESERVE BANK OF ST. LOUIS

Table 2

Summary of Intervention Survey Responses

	No. of responses	Never	Sometimes	Always
9. The following are factors in intervention decisions:				
To resist short-term trends in exchange rates	19	10.5	42.1	47.4
To correct long-run misalignments of exchange rates from fundamental values	18	33.3	44.4	22.2
To profit from speculative trades	17	100.0	0.0	0.0
Other	16	62.5	25.0	12.5
10. Intervention transactions are conducted secretly for the following reasons:				
To maximize market impact	17	23.5	35.3	41.2
To minimize market impact	14	42.9	57.1	0.0
For portfolio adjustment	11	100.0	0.0	0.0
Other	12	75.0	16.7	8.3
11. In your opinion, how long does it take to observe the full effect of intervention on exchange rates?				
A few minutes	18	38.9		
A few hours	18	22.2		
One day	18	0.0		
A few days	18	27.8		
More than a few days	18	11.1		
Intervention has no effect on exchange rates	18	0.0		

To resist short-term trends in exchange rates and the correction of long-run misalignments of exchange rates from fundamental values are important factors in the intervention decisions (policy). Further the interventions are conducted secretly to maximize market impact or to minimize the market impact.

We call an intervention secret if it has not been reported to market participants at the latest on the day the intervention was carried out by the one or two involved central banks, or not being reported at all (13).

Remarkable: The interventions takes place on the OTC market
The gold trading activity on the OTC markets is hardly transparent.

According to a LMBA study in 2011 is the volume of gold traded in the London OTC Gold Market ten times what is implied by the clearing statistics (12).

In January 2009, the G20 asked for substantial reforms to OTC markets in order to 'improve transparency, mitigate systemic risk, and protect against market abuse'. The G20 reform agenda requires standardised OTC derivatives to be cleared through central counterparties on exchange or electronic trading platforms.
Well-known shortcomings are on the so-called pre-trade transparency (information about price quotes and trade sizes is available to the two parties involved in the trade prior to executing the trade), the post-trade transparency (information about executed trades made available to market participants other than the two parties involved in the trade, or a narrow set of dealers).
Through this information asymmetry are uninformed participants at risk of making the wrong trading decisions (14).

Behind the Spot Price of Gold
The Spot Price of gold is the price of gold around the clock less just a few minutes. Actually it is an quotation price of gold between the so-called Market Makers (Citi, Goldman Sachs, HSBC, JPM, UBS, Bank of Nova Scotia, ICBC, Merrill Lynch, Morgan Stanley, Societe Generale and Standard Chartered Bank) based upon their activity in the hardly regulated OTC market. According to the LMBA OTC markets provides confidentiality as the transactions are conducted solely between the two principals involved and is this particularly important for central banks activity in the market (15). The Spot Price of gold is under control of the central banks c.s. (8). See our article of 23 September, 2016 "Behind the Spot Price of Gold."

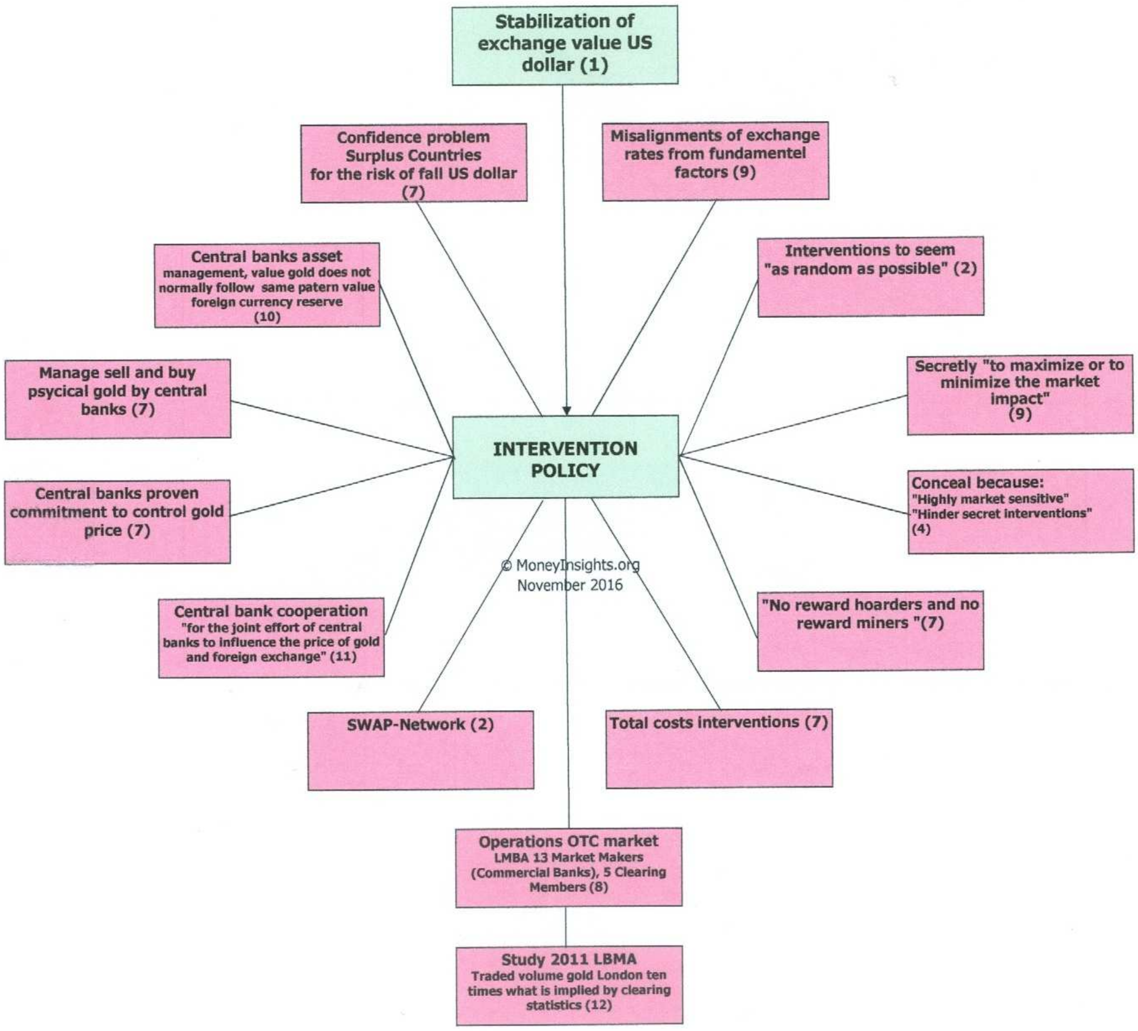
Central Bank Coordination
In 2016 the FED made a study on how central banks interact with one another in normal times and how they behave during times of crisis (e.g. The Global Financial Crisis 2007, 2008). One conclusion is

that the policy response of the central banks on global financial crisis required an extraordinary degree of central bank coordination, and will have implications for how central banks operate (and relate to each other) for generations to come (6).

4. Determinants Intervention Policy

...No transparency at all...

Based upon study we (re)constructed some Determinants from the Intervention Policy on the price of gold by central banks.



5. Conclusion

It is obvious that the central banks within the BIS network handle an intervention policy for the price of gold. Furthermore they built up an implementing organisation for the execution of this intervention policy. The interventions are secret because they are not being reported to market participants at the latest on the day the intervention was carried out by the one or two involved central banks, or not reported at all. The interventions set the Spot Price of gold.
The regulatory authorities seem to look away.

6. Note of the writer

In our paper from 20 July, 2015 we concluded that JPM in cooperation with the BIS controls the dollar gold price through interventions on the development of the dollar gold price. Overall the conclusion was that there is no free market for gold.

In our paper from 7 October, 2015 we explained that JPM and the BIS are operating agents for the BIS network to maintain the confidence in the dollar and therefore manipulate the dollar gold price.

The BIS network is the successor of the Gold Pool. The Gold Pool provided for central banks of surplus countries with large foreign exchange reserves to share the burden of interventions in the London gold market in order to keep price fluctuations within a reasonable range. The BIS network determines the intervention zone for the dollar gold price for their operating agents.

In our paper from 23 September, 2016 we explained the setting and the importance of de Spot price of gold. The Spot price of gold is the basis for many transactions in gold. Actually it is an quotation made by so-called (thirteen)Market Makers (commercial banks) and based upon their trading activity in the hardly regulated OTC-market.

(1) Audit Report 8 December, 2015 ESF Fiscal Years 2015 and 2014
(2) Economic Review March 1979 Federal Reserve Intervention Policy by R.K. Abrams
(3) The Mechanics of Intervention in Exchange Markets by A.B. Balbach (FED), februari 1978
(4) Special Data Dissemination Standard by IMF 10 March, 1999
(5) Restricted-Controlled notes Gold and Foreign Exchange Committee G-10 7 April, 1997.
(6) Study International Aspects of Central Banking 30 July, 2016 by Robert B. Kahn cs
(7) Study International Monetary and Financial Cooperation, Piet Clement (BIS), June 2006
(8) MoneyInsights.org, article 23 September, 2016, Behind the Spot Price of Gold
(9) Summary of Intervention Survey June 2001 by C.J. Neely, FED of St. Louis
(10) Site Riskbank Sweden, October 2016
(11) MoneyInsights.org, article 29 November, 2015, Speech William R. Wright (BIS)
(12) Financial Times 9 September, 2011
(13) Study Reported and Secret Interventions in the FX Markets by Michael Beine, 2003
(14) Bank of England Quarterly Bulletin 2011 Q4
(15) Letter LBMA to the Bank of England 30 January, 2015 regarding Fair Markets