

# China is Playing the Gold Game very Carefully: Covert Purchases of Gold

By [Koos Jansen](#) and [Lars Schall](#)

Global Research, December 05, 2015

[Gold Switzerland](#) 5 December 2015

Region: [Asia](#)

Theme: [Global Economy](#)

*On behalf of Matterhorn Asset Management, Lars Schall talked with one of the prime researchers when it comes to the People's Republic of China gold policy; Dutch analyst **Koos Jansen**. They discuss the many tricky details that have to be taken into account; since the Chinese gold buying is pretty much a covert operation.*

**Lars Schall:** My first question would be, during this year, the Chinese Central Bank announced its new gold position. How much does China possess now and do you think those numbers are accurate?

**Koos Jansen:** Well, they state they have about 1,700 tons right now. I do not think those numbers are accurate. I think the numbers they disclose now every month since June, they are increasing their reserves a little bit, just like Russia does, and I think this is a strategy maybe communicated between Russia and China even to slowly push for a new monetary system, international monetary system. So, if they would've disclosed they have 3,000 tons or 4,000, whatever they have or see fit to disclose, they would really rock the boat in the international sphere.

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## TRANSCRIPT

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**Koos Jansen:** Well, they state they have about 1,700 tons right now. I do not think those numbers are accurate. I think the numbers they disclose now every month since June, they are increasing their reserves a little bit, just like Russia does, and I think this is a strategy maybe communicated between Russia and China even to slowly push for a new monetary system, international monetary system. So, if they would've disclosed they have 3,000 tons or 4,000, whatever they have or see fit to disclose, they would really rock the boat in the international sphere. So, they are very careful in playing this game and they also want to be included into the SDR to internationalize the Renminbi.

That is of great importance for them, so they are finding ways to internationalize and the Renminbi being included into the SDR is one of them, to be a reserve currency, and so they don't want to make too many enemies. So, they're playing it really careful. They stated in, I believe it was June or July, they increased official gold reserves by 600 tons from 1,054 to about 1,700 and they're increasing reserves now by, you know, 15 tons a month more or less. I think it's a strategy to slowly push for a new international monetary system in which the Renminbi will have a much greater role. So, I don't believe the 1,700 number. I think they have a little bit more, between 2,000 or 4,000 tons.

I did a study once about this but it's kind of difficult because it's really one of the best kept secrets on earth, but my study indicated that they do buy about 500 tons a year. There was a small segment in the paper from Deutsche Bank that said the PBOC is buying 500 tons a year. I stumbled upon a study from a guy from the China Gold Association who had written a report in 2011 and he advised the People's Bank of China to increase its official gold reserves by 500 tons a year, so that would be about 3,500, 4,000 tons right now. Of course, this gentleman from the China Gold Association is not a policymaker but I collected a lot of hints from various places that the People's Bank of China is buying about 500 tons a year. Now, we can't prove it but it sure suggests they have more than 1,700 tons and then indirectly it suggests that the 1,700 tons they state they have is just strategy.

**LS:** Yeah, but the Chinese can buy gold covertly. I mean, your company, for example, has done a study that a huge amount of gold went off the radar in London. How can that be?

**KJ:** Yes, that's correct. That started with an investigation from Ronan Manly from BullionStar and Nick Laird from Sharelynx, and Bron Sucheki and I also helped a little bit. In the first instance, it was a study about the London bullion market and how much gold was left in London. Now, they found that in 2011, there were 9,000 tons in London in the LBMA system, let's say, within the London Ring way so that includes LBMA vaults, it includes the vault of the Bank of England, foreign central bank it's called, and then in 2015, that number dropped from 9,000 to 6,250. So, it means that 2,750 tons were removed or had left London since 2011.

Now, official foreign trade statistics indicate that the UK over this period only net exported about 1,000 tons, so that means that 1,750 tons is missing from London, let's say. So, that can be possible because what we see in international merchandise trade statistics, I should say that's the official name for goods and services crossing the border, only non-monetary gold is disclosed. So, what I do and a few colleagues of mine is we track all merchandise trade statistics from the UK, Switzerland, Hong Kong, all the gold trading hubs, also some mining nations such as Russia or nations in Africa. But all of those numbers only include non-monetary gold because the rules are that non-monetary gold must be disclosed in these reports but monetary gold is exempt from being disclosed in foreign trade statistics.

So, in this way, for example, the People's Bank of China can buy gold in London, non-monetary gold from whatever seller and they can monetize it in London and then covertly ship it home without it having to be declared at the customs department. They can do this all around the world. They can do it in Africa, they can do it in Switzerland, and they can do it in Hong Kong. Just to illustrate, Hong Kong net imported 600 tons of gold in 2013. That's a lot of gold but I think it's possible that the People's Bank of China bought a part of that gold in Hong Kong once it was imported as non-monetary gold in Hong Kong. Probably a part of it was monetized in Hong Kong and then shipped to the mainland for the official gold reserves of the People's Bank of China.

**LS:** Yes, but when it comes to gold buying as a covert operation, so to say, does the PBOC buy gold directly or is this buying through proxies?

**KJ:** I think they buy through proxies because what they buy is kind of a good kept secret, and they are very secretive about it. So, to avoid any risk of leaking, I think they buy through proxies. In any case, they buy through SAFE and maybe through CIC which are sovereign wealth funds, but even maybe through Chinese commercial banks, I don't know, but I assume they buy through other proxies.

**LS:** And does this buying take place via the Shanghai Gold Exchange?

**KJ:** No. This is the whole thing. This is what I like to talk about because a lot of analysts look at China and they count how much China is mining every year and they count how much non-monetary gold imports into China is every year. China doesn't disclose how much they import in non-monetary gold but from looking at other nations, for example, Hong Kong and Switzerland and the UK, we know how much they export to China so we can more or less figure out what they import. But that is all non-monetary gold and all the non-monetary gold which is imported into China is required to be sold through the Shanghai Gold Exchange. So, the question then is, does the People's Bank of China buy gold through the Shanghai Gold Exchange.

Now, I don't think they do. There are a number of reasons. One reason, for example, is that I think the People's Bank of China likes to buy London Good Delivery Bars, which are 400 ounce or 12.5kg in the metric system, because the gold in those bars is cheaper. If you buy a ton of gold in coins, it's more expensive than in London Good Delivery Bars. So, I think they buy London Good Delivery Bars but these bars are not being sold through the Shanghai Gold Exchange.

They can be sold but if I look at all the trade data from the Shanghai Gold Exchange, only I think, if I recall correctly, three tons have been sold in London Good Delivery Bars in 12.5kg bars through the Shanghai Gold Exchange in recent years. So, that will mean that either the People's Bank of China is not buying London Good Delivery Bars or they are not buying through the Shanghai Gold Exchange. For example, all gold on the Shanghai Gold Exchange is denominated in Renminbi and I think the People's Bank of China wants to diversify its foreign exchange reserves, which are predominantly in US dollars for gold. So, they want to sell their US dollars and buy gold.

That is not done through the Shanghai Gold Exchange. So, I made a whole list, I wrote an article about this once, about all the reasons why the People's Bank of China may or may not buy gold through the Shanghai Gold Exchange and it's kind of obvious they would not buy gold through the Shanghai Gold Exchange, **aLS**o because it would be done in clear sight. If they buy a few tons every week in the Shanghai Gold Exchange, everybody would see it, you know, and again, they would then buy all these 1kg bars. So, I think given the fact they are so secretive about it and all the reasons I think they will never buy gold through the Shanghai Gold Exchange. I do think they are able to intervene in the Chinese domestic gold market but as a main hypothesis, I'd say the People's Bank of China would not buy gold through the Shanghai Gold Exchange and from there, I try to analyze.

**LS:** Okay, but where do the Chinese try to sell their dollars and get gold in return?

**KJ:** Well, London is an example. Most gold across the world is paid for in US dollars so they

can buy it anywhere. Also, Singapore, Hong Kong, Australia, maybe they have some deals with mining companies in Africa or Australia that they covertly ship some to China mainland but it's not difficult of course to sell your dollars and buy gold in the international market.

**LS:** Yeah, and talking about gold mining projects, well the 'One road, One belt' project in Eurasia driven by the Chinese is connected already to gold. Can you talk a little bit about how this is connected to gold?

**KJ:** On the Eurasian continent, there are a lot of clubs cooperating at the moment and that is kind of interesting. Maybe the biggest club is the 'Silk Road Economic Project' also called the 'One Belt, One Road' project initiated by the Chinese President – I believe it was in 2012 but in the last year, it gathered steam. There are about 60 countries along this Silk Road and his intention is to have more cooperation on the political and economic fields now. The Silk Road is a big project and there's also a Silk Road fund but underneath this Silk Road project, we have the Asian Infrastructure Investment Bank which has 57 founding members among which a lot of western countries, a lot of European countries.

There is also the Eurasian Economic Union which consists of Russia, Belarus, and Kazakhstan. That is not officially a part of the Silk Road project yet but these are clubs that are all gaining ground on the Eurasian continent. You then have the Shanghai Cooperation Organisation and all these clubs are also starting to cooperate a little bit.

There's also President Putin who said already that his Eurasian Economic Union will cooperate with the Silk Road Economic Project so that is one. And now this year, the Chinese have disclosed that there also will be a Silk Road Gold Fund which is led by the SGE and is meant for more cooperation on the Eurasian continent obviously in mining exploration, gold trading, and things like that. So, that is a really significant development and the SGE also said that it will facilitate gold buying for foreign central banks. So, I can imagine countries like Kazakhstan, for example, buying gold through the Shanghai Gold Exchange, Shanghai International Gold Exchange, I should say, in the future.

So, this is the intention of the Silk Road Gold Fund. We also saw some little signs of cooperation earlier this year. Russia's biggest mining company, Polyus Group, started a cooperation with China's biggest mining company, China National Gold Group. I just wrote an article about this, Polyus sells most of its gold so it outputs through VTB Bank which is a Russian bank and VTB Bank also became a member of the Shanghai Gold Exchange last week. So, likely more gold from Polyus will be sold through VTB Bank on the Shanghai Gold Exchange. The volume of the Shanghai International Gold Exchange is still very low and the Shanghai International Gold Exchange is really meant for the world to sell its gold in Renminbi to other countries. The volume is very low at the moment so we can say it has failed up until now but who knows what the future will hold.

**LS:** Isn't it interesting, you've mentioned the Shanghai Cooperation Organisation which was launched in the summer of 2001 that many of the members are buying gold actively, that many of the countries that are intended to be members of the SCO one day that they are also buying gold, for example, Turkey, and that many of those countries, they have the majority of all the gold that is in the ground, in the soil still to produce?

**KJ:** Well, first I'd like to say that Turkey is not buying gold. Turkey has a special system in which commercial banks offer Turkish citizens to deposit their gold. The Indian system, which has been launched now is kind of based on the Turkish system. So, in Turkey, people

can go to a bank and they can deposit their gold and get an interest on their gold. Of course, they risk losing their gold, but this gold is being collected by commercial banks can be used by commercial banks as reserve requirements at the central bank. So, they use this gold from the citizens as a reserve requirement at the central bank. The central bank counts this gold as their official gold reserves, so the Turkish Central Bank is not buying any gold. They just double count the gold from the citizens.

**LS:** Thank you for underlining this.

**KJ:** Yes, I should write a new article about this because I think the system is exactly the same now or being launched now in India. The Indian Central Bank also has said that the Indian commercial banks can use the gold in deposit from the citizens as a reserve requirement. So, I don't know if they're going to count that gold also as official gold reserves but it's very worth watching. So, the next question was about the Shanghai Cooperation Organisation, yeah. Of course, those nations are buying gold and I see a lot of gold in the wider Silk Road region.

If we look at Asia and Europe, for example, a lot of countries in Asia are buying gold and then we have, for example, in India, the people are buying a lot of gold, about 900-1,000 tons a year. In other Asian countries, the central banks are buying gold which is very significant because that is like, you know, we are diversifying away from the US dollar. I don't need to tell our listeners this; a lot of buying is happening on the Asian continent. On the European continent, these central banks already have a lot of gold but what they're doing is they're repatriating their gold from the UK, from the Bank of England, and from the Federal Reserve Bank of New York in the US. So, I think both continents, Europe and Asia are focused on gold and slowly moving away from the US dollar, albeit that the Europeans are not yet buying. They're repatriating because they have already significant amounts of gold. The Asians are buying.

**LS:** Recently, Peter Mooslechner, an official of the Central Bank of Austria said that the Asians are more active in the gold market now and that they use their gold to influence the price or actually he said to intervene in the market. Do you have something to say on those statements that he made?

**KJ:** Yeah. Well, actually I found his interview very interesting. I don't really know what he meant by intervening because he also said that, you know, we gold analysts immediately think about gold price manipulation. I don't know if all those countries he mentioned are manipulating gold price because he also mentioned the euro system and the ECB are intervening into the gold markets, just like the Asian countries. I'm not sure what he meant by that.

**LS:** Yes, but you know that I've asked him some specific questions.

**KJ:** Yes, I know.

**LS:** It's their policy not to provide answers to any questions that relate to their strategy with gold or other central banks strategy with gold.

**KJ:** Yes, of course, if you ask a central banker about gold, he will never answer you. I've found that all across the world which is a signal in itself we can think, but I didn't really focus on the comments of Mooslechner on the intervening parts which he said. I found more

interesting what he said about repatriating gold and about Europe maybe even buying gold if the Chinese economy is going down.

The world is entering a recession again. I found that very interesting and also because at one point he said that European countries, more and more European countries are repatriating because of economic nationalism which is a contradiction to what he said a minute before and that was that the Austrian Central Bank was repatriating because of a concentration risk at the Bank of England. So, clearly this contradiction indicates that he is not repatriating because of a concentration risk at the Bank of England but because of other reasons. Now, also this year, the General Court of Auditors in Austria, they released a report in which they disclosed that the Austrian auditors were not allowed to audit their gold in England in the past years in between 2009 and 2013. That is of course one of the real reasons why Austria is repatriating is because the gold is not safe at the Bank of England or, you know, for other countries like the Netherlands. The gold is not safe in New York. That's why they are repatriating and so that was my takeaway from the interview with Mooslechner.

**LS:** Yes, and is it your perception related to the German case that the Bundesbank is following a policy of economic nationalism. Don't you think that it is very reluctant and that it does what it does only because there was public pressure?

**KJ:** That's a good question. Of course, it also has to do with public pressure but I don't think the Bundesbank is only repatriating because of public pressure. I think they do it because of their own interests, bearing in mind, I believe it was in 2001, the Bundesbank repatriated about 1,000 tons from the Bank of England in secret. Nobody knew about it so there was no public pressure at the time and they repatriated the gold even still from the Bank of England. The same goes for the Netherlands. They repatriated.

The Dutch Central Bank repatriated not really because of public pressure. I mean, there was some, you know, I submitted a freedom of information act (FOIA) request once and there were some talks in politics. Of course, that happened after the economic crisis, you know, chatter about gold was started but I don't think it was public pressure in the Netherlands or in Germany that led them to repatriate the gold. I think it's their own interest. The second question of course is, so why do they take so long and why don't they repatriate all the gold. Now, just like I said previously about Asia, I think they do this so slowly because it's such a sensitive subject. Maybe the gold indeed is not all there anymore so that's why they have to do it very gently. We can also imagine that if, for example, the Netherlands, Austria and Germany were to repatriate all their gold all at once then it would of course lead to instant shock in financial systems. So, I think it's on purpose that they do it slowly but it's speculation.

**LS:** However, the Germans intend to leave roughly half their gold position in New York and London. This is now the official position of the Bundesbank that they want to leave it there so they are able to react to a real currency crisis if that happens. Do you have to have the gold in London and in New York for such a purpose?

**KJ:** I would say no. I mean, if there would be a currency crisis, people would rush to gold and your gold would become more valuable and you would like to have it at home, not in England or New York. Only if there was a crisis and you want to sell gold, you would like to have gold in London, but how I look at it, I think it's better with economic turmoil up ahead to have your gold at home than in England.

**LS:** Yes, and the IMF says that gold, monetary gold, physical bullion gold is the only financial asset with no counterparty risk.

**KJ:** Yes, with no counterparty risk. This was stated in the balance payments manual number six. Yeah, yeah. I think those things are really significant and, you know.

**LS:** Yes, but in order to be such a financial asset, you really have it in your own possession, on your own soil, right?

**KJ:** Right, right. Oh, sorry, you were referring to the previous question. – You’re absolutely right. If you talk about gold and gold is the only asset with no counterparty risk, you’d need it at home and of course it does have a counterparty risk if it’s in London or in New York. It’s as simple as that. Yeah, you’re right.

**LS:** Now, another question would be that China is a big producer of gold but the production doesn’t leave the country. Where does it go to?

**KJ:** I think to the private sector in China. Before 2002 when the Shanghai Gold Exchange was launched, the People’s Bank of China had the monopoly in the Chinese domestic gold market. So, all the domestic mining output was sold to the People’s Bank of China and then it was distributed to a few designated jewelry shops or to maybe the coffers of the PBOC. So, before 2002, all the gold that was mined in China flowed through the People’s Bank of China but since the Shanghai Gold Exchange was launched in 2002, most of the gold, I would say 99% of the gold mined in China is being sold through the Shanghai Gold Exchange, and then what I just spoke about in one of my previous answers is that I think the private sector are the buyers on the Shanghai Gold Exchange in China. So, it does not really go to the People’s Bank of China, maybe still a little bit is going to the People’s Bank of China because maybe they still have some covert mines operating in China but actually most of the conventional output is being sold through the Shanghai Gold Exchange.

**LS:** Koos, thank you very much for this interesting conversation.

**KJ:** Okay, thank you very much, Lars.

***Koos Jansen** started his financial blog “In Gold We Trust” ([ingoldwetrust.ch/](http://ingoldwetrust.ch/)) in 2013. His curiosity about the gold market made him gather an incredible amount of information in a relatively short period of time in particular about the Chinese gold market and he gained much insight into the role of gold in international financial markets. He now shares his information and experiences vividly with a larger audience via his blog at Bullion Star – see here: <https://www.bullionstar.com/blogs/koos-jansen/>*

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