Alchemist

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LBMA

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EDITORIAL
REDEFINING MEMBERSHIP

BY DAVIDE COLLINI, CHAIR OF LBMA'S MEMBERSHIP COMMITTEE AND HEAD OF EMEA METALS AND AGRICULTURAL SALES, BNP PARIBAS

Historically, we've not been particularly good at articulating the benefits of membership of LBMA. There still persists in some quarters the perception that we're an exclusive club. For example, some people still think that membership is restricted to UK-domiciled companies even though that rule changed several years ago.

LBMA IS THE VOICE PIECE, THE STANDARD SETTER AND THE QUASI REGULATOR FOR THE GLOBAL OTC PRECIOUS METALS MARKET

REACHING OUT

At the start of 2019, the Board set a number of new targets for LBMA as part of its new three-year strategic vision. For the Membership Committee, this requires us to extend our outreach to engage more closely with sectors of the market where LBMA is under represented, for example, the mining, investment and central bank communities, as well as reaching out to the key Asian markets through the establishment of LBMA Asia. Our message is that LBMA is the voice piece, the standard setter and the quasi regulator for the global OTC precious metals market.

FROM HERE TO INTEGRITY

As well as the integrity of LBMA, we also need to ensure the integrity of our members. All members are required to attest to the Global Precious Metals Code (the Code), which sets out a common set of principles to promote the integrity and effective functioning of the global OTC market. We have also strengthened the criteria for membership. A 12-month track record in the bullion market as evidenced by three attesters remains a requirement of all applications. However, the quality control element is now driven by enhanced due diligence processes.

We are also undertaking an overhaul of our membership structure and classifications this year in order to deliver a more transparent and streamlined structure to include new categories of membership. We will keep you posted on the outcome.

SETTING THE STANDARDS

It's not just about reaching out to new potential members, we also need to do a better job of reminding existing members about all the hard work and initiatives that we are undertaking on their behalf. One of the key strengths of LBMA is establishing best practice and setting standards through its Responsible Sourcing Programmes, the Good Delivery List and the Code. These standards deliver integrity and credibility to the industry, which all LBMA members benefit from.

SHAPING THE FUTURE

LBMA also represents and acts in the interests of the whole market. This was demonstrated when LBMA stepped up to the plate in the market's darkest hour, when the fixing companies stood down as administrators of the price auctions. In addition, the Gold Bar Integrity initiative is designed to deliver new technologies to bolster further the integrity of the physical market.

Members of LBMA can actively participate in such initiatives and help shape the future of the market.

NEW MEMBERS' PORTAL

LBMA also provides legal advice on a raft of regulatory changes which have impacted and continue to impact on all aspects of the market. For example, we are leading the way in lobbying the European regulatory authorities to abandon the 85% haircut in respect of NSFR and we are using the new trade reporting data to support our case. Our new members' portal, MyLBMA, which we have just launched, is designed to enhance the member experience and provides the gateway to regulatory updates as well as a wealth of other unique member content including webinars, member briefings and publications.

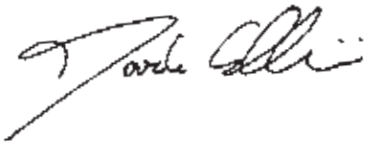
WE ARE ALSO UNDERTAKING AN OVERHAUL OF OUR MEMBERSHIP STRUCTURE AND CLASSIFICATIONS THIS YEAR IN ORDER TO DELIVER A MORE TRANSPARENT AND STREAMLINED STRUCTURE

NETWORKING AND SOCIAL EVENTS

Members can also take advantage of discounted rates to attend our annual precious metals conference and our biennial A&R event, as well as complimentary events including webinars and our annual party and dinner (note that this is no longer a biennial event!). This year to celebrate the centenary of the gold price we are running a series of complimentary events. We hope to see many of you in attendance.

OUR MISSION

Our mission is to ensure the highest levels of integrity, transparency and leadership for the global OTC market. If you are not already a member, come and talk to us. We'd love to tell you more about LBMA and how we can benefit you.



ISSUE HIGHLIGHTS

Front cover - The Goldkammer Frankfurt. The treasures in Gold from the Seas, document both the conquest of the New World by Spanish conquistadors.

Inside the GOLDKAMMER Frankfurt

BY DR. NADJA TOMOUM, DIRECTOR, GOLDKAMMER FRANKFURT

A visit to the Goldkammer Frankfurt is an encounter with the most magical of all precious metals. Nowhere else in the world can you discover so many different facets of gold.

The metal has stirred human desire ever since one of our early ancestors saw the first piece of gold glittering on a riverbed and could not resist reaching out for the temptingly shiny object. This chance discovery began humanity's untiring search for gold and fired its ambition to harness its properties in various ways. Frankfurt's latest museum brings to life the history of gold for all of the senses. The Goldkammer has been conceived as a museum of art and cultural history, and as an information centre for gold's multifaceted uses as both a material and precious metal.

HG MERZ

The entrance is located in a landmarked mansion in Frankfurt's Westend district within walking distance of the Alte Oper opera house. The renowned architectural office of HG Merz was commissioned to design the museum and has created a focused exhibition that offers visitors the impressive experience of being at a show. Despite its small size, the Goldkammer provides all the amenities of a modern museum, including a permanent exhibition, a space for special exhibitions, an exclusive events room, a café, a bistro and a museum shop.

GOLD MINE

Visitors are prepared for the unique world of experience while descending to the museum in the elevator. A sequence of small treasure rooms on the first underground level, spanning a period of over 6,000 years, bring more than 500 objects to life. With walls of rough natural stone, the rooms in the Prologue section have been designed to resemble a gold mine. This area is dedicated to the geology of gold – its origins, emergence and extraction. It focuses on gold as a material while providing a tactile experience of the precious metal. Digital screens and the corresponding exhibits provide clear explanations of complex topics.

Bronze age gold smith's masterpiece gold bracelet formed from alluvial gold.

6,000 years

500 objects

A sequence of small treasure rooms on the first underground level, spanning a period of OVER 6,000 years, bring more than 500 objects to life

EARLY CULTURES

From the Prologue, visitors enter the main section of the Goldkammer, which presents gold from various cultures. Here, in Early Cultures, the rammed earth walls lend the objects a mysterious air and the great skill of prehistoric goldsmiths comes into view. Cast ring idols from south-eastern Europe are eloquent proof that the beginnings of the gold industry lay in the Copper Age. Unique artifacts made by the Scythians, Thracians and Achaemenids provide a glimpse of goldsmithing in the regions around the Black Sea. In the first millennium BC, their artisans engaged in a lively cultural exchange that is reflected in a shared formal language – particularly in animal symbolism.

An impressive presentation of 300 standard gold bars from the Rothschild & Co. Collection

An unrivalled find is the hoard of a Bronze Age goldsmith who lived in central Europe. His masterpiece is a solid gold bracelet forged from alluvial gold. In *Piece of Gold – Piece of Money*, gold is presented as a sought-after object of exchange and a means of payment. In the sixth century BC, the Lydian king Croesus popularised the use of silver and gold coins imprinted with his state seal and thus guaranteed the stability of the money in circulation.

FROM ANCIENT TO NEW WORLDS

The unique objects in *Ancient Worlds,* including the finely wrought bust of the Roman emperor Licinius I, tell of power, honour and prestige in ancient Greece and Rome. *El Dorado*, by contrast, shows the artistic and technical skills of ancient American goldsmiths. A gold mask made in Colombia is a true masterpiece of pre-Columbian goldwork and was meant to transform its wearer into a divine figure of light. The treasures in *Gold from the Seas*, which were recovered from sunken galleons, document both the conquest of the New World by Spanish conquistadors and the accompanying rise in trade and economic activity in Europe, triggered by the enormous influx of precious metals from the Americas. Driven by the thirst for adventure and gold, treasure hunters salvaged precious cargo that had been lost for 400 years.

THE UNIQUE OBJECTS IN ANCIENT WORLDS TELL OF POWER HONOR AND PRESTIGE IN ANCIENT GREECE AND ROME

ROTHSCHILD COLLECTION

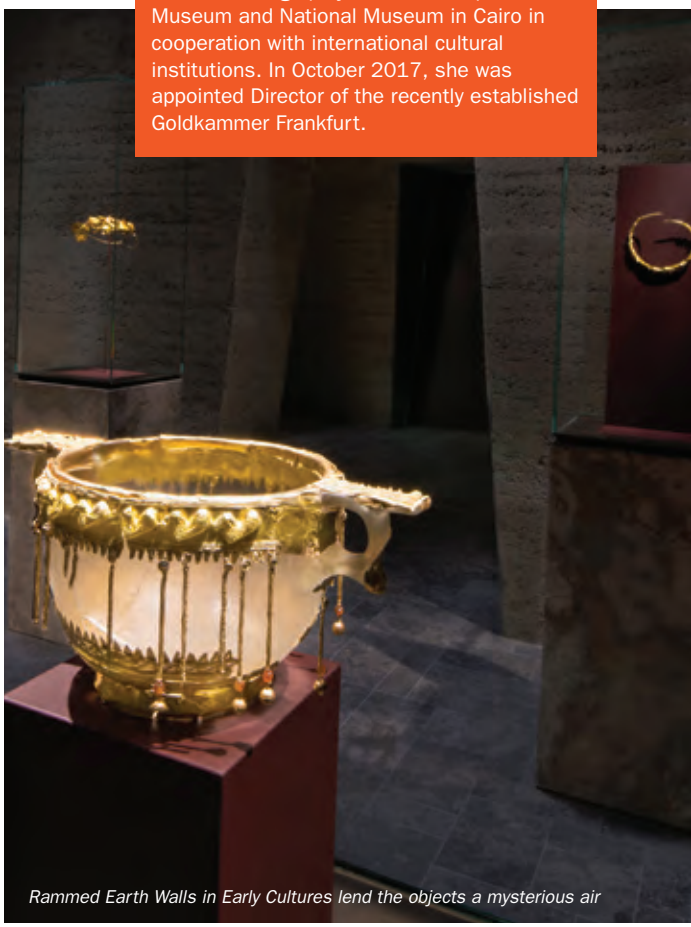
The path through the Goldkammer culminates is an impressive presentation of 300 standard gold bars from the *Rothschild Collection*. These bars, collected from different countries, embody gold's international significance as a popular investment, collector's item and store of value. An animated film recounts the economic history of gold over the last 6,000 years.

VISITOR AIDS

The Goldkammer is designed for young and old. Its mission is to impart interesting and surprising facts about gold while generating enthusiasm for the precious metal. In the show, visitors receive a wealth of information about the exhibited objects, their contexts and background. Enthusiasts can learn more about the objects with the help of a free museum app or an exhibition companion available at the ticket desk. These aids, however, do not detract from a personal engagement with the artworks. Before regular opening hours on workdays, the Goldkammer is reserved for school classes and other groups, and it provides activities for its youngest visitors. Following a vein of gold that runs through the display rooms, they can track down Aguila, the museum's mascot, who introduces them to select objects with the help of fairytales audible on a smartphone.

The museum shop carries a select range of products, including the Goldkammer Jewellery Collection, postcards showing various images from the collection, exhibition catalogues and additional souvenirs. The café and bistro serve special culinary delights in a cozy atmosphere and, during the summer months, visitors can eat their snacks on the terraces on the ground and first floors. In addition, the Goldkammer offers a bookable all-round package of services for exclusive evening events.

GOLDKAMMER IS DESIGNED TO IMPART INTERESTING AND SURPRISING FACTS ABOUT GOLD WHILE GENERATING ENTHUSIASM FOR THE PRECIOUS METAL



Rammed Earth Walls in Early Cultures lend the objects a mysterious air

From museum tours and a versatile multimedia wall to catering, interested parties can design their personal programme to suit their tastes. Our high-tech equipment and special atmosphere guarantee a festive occasion. The Goldkammer Frankfurt wishes its visitors an entertaining journey into the world of gold!

Nadja Tomoum graduated from the Ludwig Maximilians University of Munich with a Ph.D. in Egyptology. She was sent by the Federal Ministry for Economic Cooperation and Development to Egypt to work as a museum expert for the Ministry of Antiquities and the private sector. From 2006 to 2015, she spearheaded pioneering exhibition and cultural heritage projects at the Coptic Museum and National Museum in Cairo in cooperation with international cultural institutions. In October 2017, she was appointed Director of the recently established Goldkammer Frankfurt.

Photos were taken by Hubertus Hamm and the Goldkammer jewellery collection produced by Kevin Barnes.

100 GOLD PRICE CENTENARY

GOLD INVESTING/ HOARDING IN THE FREE 1930s LONDON MARKET: 1931-1939

BY FERGAL O'CONNOR, LECTURER IN FINANCE, CORK UNIVERSITY BUSINESS SCHOOL

The third instalment of Fergal's academic analysis of the gold price which focuses on the years leading up to the start of World War II.

On Sunday, 20 September 1931, the UK Treasury announced that it had advised His Majesty's Government to depart from the Gold Standard (Government, 1932). This action reinaugurated a free market for gold in London following six years on the Gold Standard. The London gold market would continue to operate (relatively) freely until 3 September 1939, as World War II broke out.

This eight-year period saw increased interest in gold from investors, with M. Eccles (1936) at the US Federal Reserve pointing to "private hoards" of gold being worth approximately $2 billion in total globally in 1936, which in today's terms would be about $483 billion based on Economic Share. The Federal Reserve (1954) further reported that between 1931 and 1954 about $21 billion of gold had been purchased by private individuals, or $1.1 trillion in terms of modern Economic Share. The total value of gold held by private investors in 2018 came to approximately $1.69 trillion based on World Gold Council estimates – indicating that investors in the 1930s held gold in similar proportion to investors today.

WHERE PREVIOUSLY ONLY ONE LINE HAD BEEN AVAILABLE BETWEEN ALL THE PARTICIPANTS EACH PARTICIPANT WAS PROVIDED WITH A PHONE

Gold ownership during this period was always referred to as 'hoarding' whether by national authorities or the bullion banks themselves. Montagu's Annual Bullion Letter in 1932 says that the London market gold price was not just set by reference to the US fixed gold price and the dollar-sterling exchange rate, but in fact, the London Fixings Gold Price frequently went above that price due to "Foreign enquiry for Hoarding".

Harvey (2008) discusses the evolution of the form of the London Gold Fixing in detail since its 1919 inception and points to the 1930s market as being the period when it began to resemble what we would think of today as the Fixing. Telephones became commonly used during the Fixing. Where previously only one line had been available between all the participants, now as speculation caused prices to change more frequently, each participant was provided with a phone in order to be able to discuss the changes with their home office.

AN INVESTOR'S VIEW OF GOLD IN THE 1930s

One major reason why I wanted to collect data from the 1930s was in order to examine whether the roles that gold plays in an investor's portfolio today (as a diversifier and a safe haven) are the same as the roles it played before 1968. It is possible that gold's current investment characteristics are a short-term phenomenon which might not continue going forward, if the conditions since 1968 were atypical. However, if gold acted in a similar way in the 1930s as it does today, this would make a strong case for gold to be included in investment portfolios going forward.

In order to assess gold's long-term investment case, I have also collected the first published daily index of equity prices for the London market, The Financial News 30 (FN30) Equity Index, which was first published in 1930. Figure 1 on page 7 shows the changes in the values of both over this period in which gold floated freely.

Gold outperformed equities significantly over the whole period for holders of both. The gold price increased 98% in total, with equity prices increasing 51%.

Fergal O'Connor is a lecturer in Finance at Cork University Business School and was previously a lecturer at the University of York. His research on Precious Metals began when he was awarded the 2011 LBMA PhD Bursary for the study of the London Gold Market and he has gone on to publish a range of research on the topic. Currently, his research focuses on building a clear picture of the operation of London Bullion Market from its inception in 1919, as well as a daily price series for gold and silver.

FIGURE 1: GOLD PRICE (£ STERLING) & FN30 EQUITY INDEX

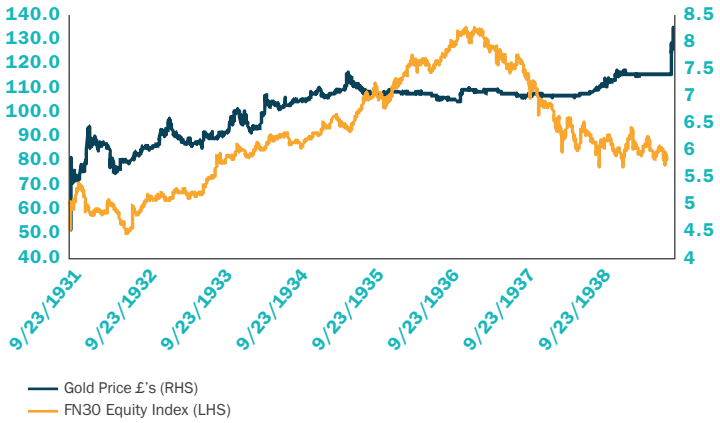


FIGURE 2: WORST DAYS ON THE LONDON STOCK MARKET

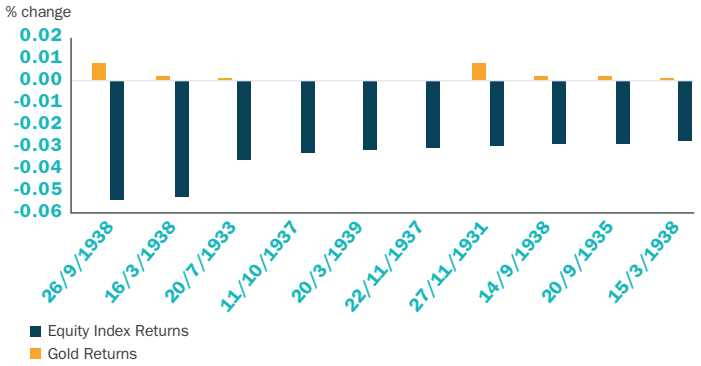


Chart above reflects the daily change in gold and stocks

As in modern markets, gold price changes had a very low correlation to changes in the value of the equity index, at about 0.21%. Gold therefore still fits well in an investor's portfolio as a diversifier.

We can also look at how the gold market reacted to sharp movements in the stock market in order to assess whether it might have been a safe haven in the 1930s. Figure 2 looks at the 10 worst days on the London equity market and what gold returns were on the same day.

On a number of these days, the gold price didn't change at all and, on every other day, gold's value increased slightly, making it exactly what investors would have looked for in a safe haven asset. If we expand our view out to the 25 worst days for equity investors, there are only two in which gold's value falls and, on both of those occasions, the Gold Fixing Price fell by less than 0.2%, while the FN30 Equity Index fell by over 2%.

The gold market of the 1930s seems to have had some similarities to the post-1968 market. More detailed research is needed, and I am currently working with colleagues on papers looking at gold as a diversifier in a portfolio of stocks and bonds during the 1930s, as well as a more detailed analysis of gold as a safe haven.

If this research is of interest please feel free to follow Fergal on Twitter at @a_fergal for updates.

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2019 CENTENARY OF THE FIRST LONDON GOLD PRICE

BY AELRED CONNELLY, PR OFFICER, LBMA

2019 marks the centenary of the first London gold price, now known as the LBMA Gold Price. In an ever changing world, it is important not only to recognise this important achievement, but to look forward to the next 100 years.

Throughout its continued recognition as the globally established benchmark, there have been significant changes to the transparency, oversight and participation in the price auction. In 2015, ICE Benchmark Administration (IBA) was appointed the first independent administrators of this regulated benchmark. Direct participation has tripled from five to 15 entities, including the addition of three Chinese banks.

To mark the centenary of the price, LBMA has arranged a series of events during 2019.

WHAT'S PLANNED FOR 2019?

SEMINAR & COCKTAIL RECEPTION, 12 SEPTEMBER

To be held on the centenary of the first gold price, in the current Rothschild & Co building, which was built on the site of (the second) New Court, St Swithin's Lane, where the first gold price was set. We would like to thank Rothschild & Co for their support in hosting this event. There will be some items from the Rothschild collection on display which will be accompanied by a talk. In addition ICE Benchmark Administration (IBA) will deliver a presentation about the gold price auction.

GOLD TALK, 27 SEPTEMBER

Ruth Crowell, LBMA Chief Executive and Paul Fisher LBMA Chairman, will deliver a joint talk at the Bank of England on the history of the gold market.

SEMINAR & GALA DINNER, 3 DECEMBER

Takes place in the historic surroundings of the Goldsmiths Hall in the heart of the City of London. A seminar will also be held earlier in the afternoon, details to follow.

COIN COMPETITION

We have received some excellent entries for the competition to design a silver 1oz medallion to commemorate the centenary. The winning entry will be judged by a panel of industry experts. The winning design will be produced in sufficient quantity as a gift for all those attending the centenary dinner in December.

GORDON'S BROWN BOTTOM, 20 YEARS ON

BY ADRIAN ASH, DIRECTOR OF RESEARCH, BULLIONVAULT

Image: Brown and Blair taken at the Labour Party Conference 1999

July 2019 marks 20 years since the UK began its infamous gold auctions, more than halving the nation's gold reserves inside three years. The decision and its timing – announced two months in advance – knocked prices 10% lower before the first sale began, on 6 July. Why would a seller want to do that? And if the Bank of England was selling, on orders from No.11 Downing Street, who on earth wouldn't?

BACKGROUND

"Conspiracy theories are widely circulating in the City," said Conservative MP Peter Tapsell to Parliament in June 1999, berating the New Labour government for planning to sell three-fifths of the UK's 715-tonne holdings. Internet chatrooms also lit up with rumours that "famous foreign finance houses" were heavily short, bribing their old Oxford college friends (now at the Treasury) to kill any price rise. Analysts, in these very pages, said Chancellor Gordon Brown was in fact rushing to sell before he took Britain into the new euro currency without asking voters.

MORE THAN 1/5 OF THE UK TREASURY'S OWN GOLD WAS OUT ON LOAN

HEDGING AND SHORT-SELLING

The Bank of England's then Head of Foreign Exchange, Clifford Smout, denied any conspiracy "with persons known or unknown!", in an article here in *The Alchemist,* but the sales still looked "catastrophic" to tabloid front pages, "bloody unhelpful" to gold-mining bosses, "appalling" to most London dealers and horrific to reserve managers across the Channel. Yet, if there had been a conspiracy to kill gold, each of these groups would have been implicated.

Borrowing gold in London, lent by European central banks seeking a yield, helped "scapegoated funds and lamented mines to stave off closure" throughout the 1990s, as Andy Smith (then at UBS) noted. Hedged by borrowing and selling well over one year's full output, global mine production set a run of new records even as prices kept falling. But central banks as a group had lent out half as much again, giving speculators perhaps 1,500 tonnes to play with. Indeed, more than a fifth of the UK Treasury's own gold was out on loan in 1999, according to BoE data, potentially helping short sellers front-run July's sale after the UK Government's announcement on Friday, 7 May. As for the financial press, Brown's move just confirmed their disdain for bullion.

"The death of gold" had in fact been splashed across the *Financial Times* 18 months earlier, back when the BoE's then Governor Eddie George mused how – what with Belgium, Canada and the Netherlands selling 1,590 tonnes between them since 1990, and Argentina plus Australia selling 290 tonnes in 1997 alone – the new European Central Bank might not bother keeping any bullion from the 11 founders of the forthcoming single euro currency. The ECB eventually decided to keep 15% of its members' subscriptions in gold, but that left half their aggregate hoard of 12,500 tonnes unneeded.

RUSH FOR THE EXITS

April 1999 then saw prices sink to near two-decade lows when Switzerland, the fifth-largest holder of gold, narrowly passed a referendum revoking the franc's role as the last gold-backed currency, green-lighting the sale of 1,300 tonnes. The next week, the International Monetary Fund joined the queue, "practically unanimous" in backing calls (led by Gordon Brown) to cut the world's third-largest holdings and write off Third World debt for the Millennium.

1. Note manufactured products such as jewellery come under a different chapter heading (7113, for example).

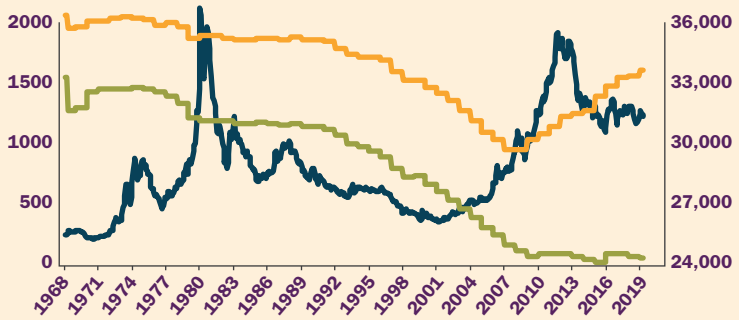
Ten days later, the UK Treasury stunned the market with its plan to "better balance" Britain's foreign exchange portfolio, selling 55% of its gold to buy more dollars, euros and yen for its Exchange Equalisation Account.

KEN CLARKE WANTED TO MAKE THE SAME ERROR BUT GAVE UP IN THE FACE OF BANK OF ENGLAND STALLING

Coming from the nation that had "invented the gold standard", as consultancy Virtual Metals put it, the news sent gold down to 18 fresh 20-year lows inside three months, costing the EEA nearly $43 million on the first 50 tonnes sold; versus 1999's average price before the announcement. Posterity hasn't recorded who coined the phrase "Brown Bottom" (sometime before 2007, according to Google), but 20 years ago this summer, it applied more to market participants than to gold's then tumbling price. Because, as Kamal Naqvi (then at Macquarie Equities) told the FT: "The ultra negative view is justifiable; the British are looking to sell before everyone else."

Gordon Brown at least managed to achieve that (see Figure 1). Hindsight also says that selling gold near its cheapest real prices in history probably wasn't his worst policy mistake as New Labour's "prudent" Chancellor. (Conservative predecessor Ken Clarke wanted to make the same error, but has said he gave up in the face of Bank of England stalling.) Brown's raid on dividend tax credits permanently reduced the nation's private pension provision. Dismantling City oversight by the Bank of England, and instead imposing a new, complex and wholly inadequate regulatory regime, also runs close as does his support for Tony Blair's disastrous war in Iraq. But either way, the gold sales decision and timing look wilful, if not vindictive.

FIGURE 1: OFFICIAL GOLD HOLDINGS VS. REAL PRICE



Gold adjusted for inflation to 2019 dollars per ounce (left axis)
Developed West + IMF,BIS, ECB (tonnes, right axis)
Total reported worldwide (tonnes, right axis)

Source: BullionVault via WGC, LBMA, St.Louis Fed

GOLD VS GREENSPAN

Unnamed sources have long told the press that the Treasury's move was strongly opposed by the BoE. In public, the Old Lady would only note coldly that it was "a political decision", and her authorised biography of 2017, David Kynaston's *Till Time's Last Sand*, doesn't deign to mention the affair. But what you think starts with where you sit and, at the end of the 20th century, most people outside London's bullion market could see nothing beyond a relentless decline for gold, both in purpose and price.

Not used for circulating coin since the 1930s, and cut out of the world's monetary system over the following four decades, the metal had lost 80% of its real worth from the 1980 peak, failing to beat inflation (let alone equities) and falling back to its all-time lows compared to the value of world economic activity (see Figure 1).

The technocrats who had replaced gold, in contrast, were enjoying a bull market.

"The twilight of gold makes sense," wrote Niall Ferguson in *The Cash Nexus*, his history of debt and money published in 2000. "[It] has a future," the Harvard professor (then at Oxford) went on, "but mainly as jewellery ... in parts of the world with primitive or unstable monetary and financial systems." Put another way, "Who needs gold when you've got Alan Greenspan?", as the *New York Times* asked of the US Federal Reserve's 'Maestro' just three days before the UK's historic announcement.

On the day itself, and amid the first tech stock bubble, New York was abuzz with the investing tip website, *TheStreet's*, forthcoming float. To get in on the deal, singer-actress Barbra Streisand reportedly chased the dotcom's CEO with free concert tickets (in 1978, her friend Bette Midler had apparently demanded payment for a tour in gold krugerrands); the stock doubled on its debut the following Tuesday.

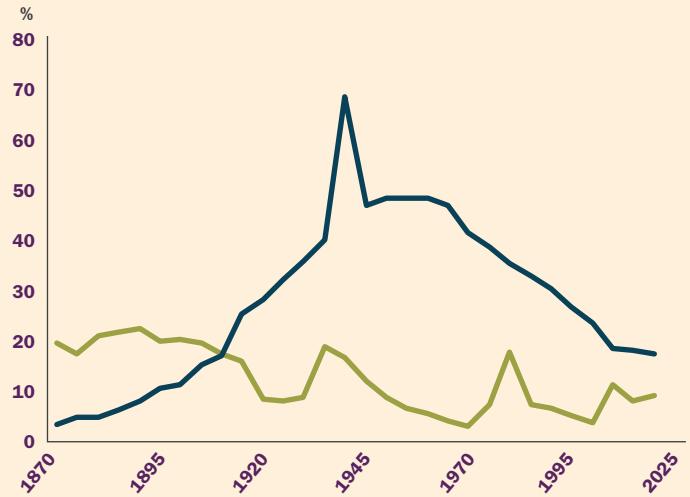
Next to such dynamism, those unrusting bars losing value in central bank vaults looked a very "barbarous relic" as John Maynard Keynes had called gold seven decades before, railing against the rules and restrictions of the Gold Standard.

THE ULTIMATE CONSPIRACY

Glancing back at gold's dramatic revaluation of the past 20 years, it's hard not to wonder if – conspiracy of conspiracies! – Brown and his bright young team (the two Eds, Balls and Miliband) weren't themselves heavily long in spring 1999. Bullion prices rose well over five-fold in dollars, euros and yen by the peaks of 2011-2013. Against the British pound, gold today trades more than six times higher. More instantly, the Treasury's announcement proved so awful for gold prices that it brought the threat of uncontrolled central bank selling to a head, jolting the rest of Europe into adopting and adapting the same strategy of 'tell then sell' with a public agreement to cap sales for the next five years.

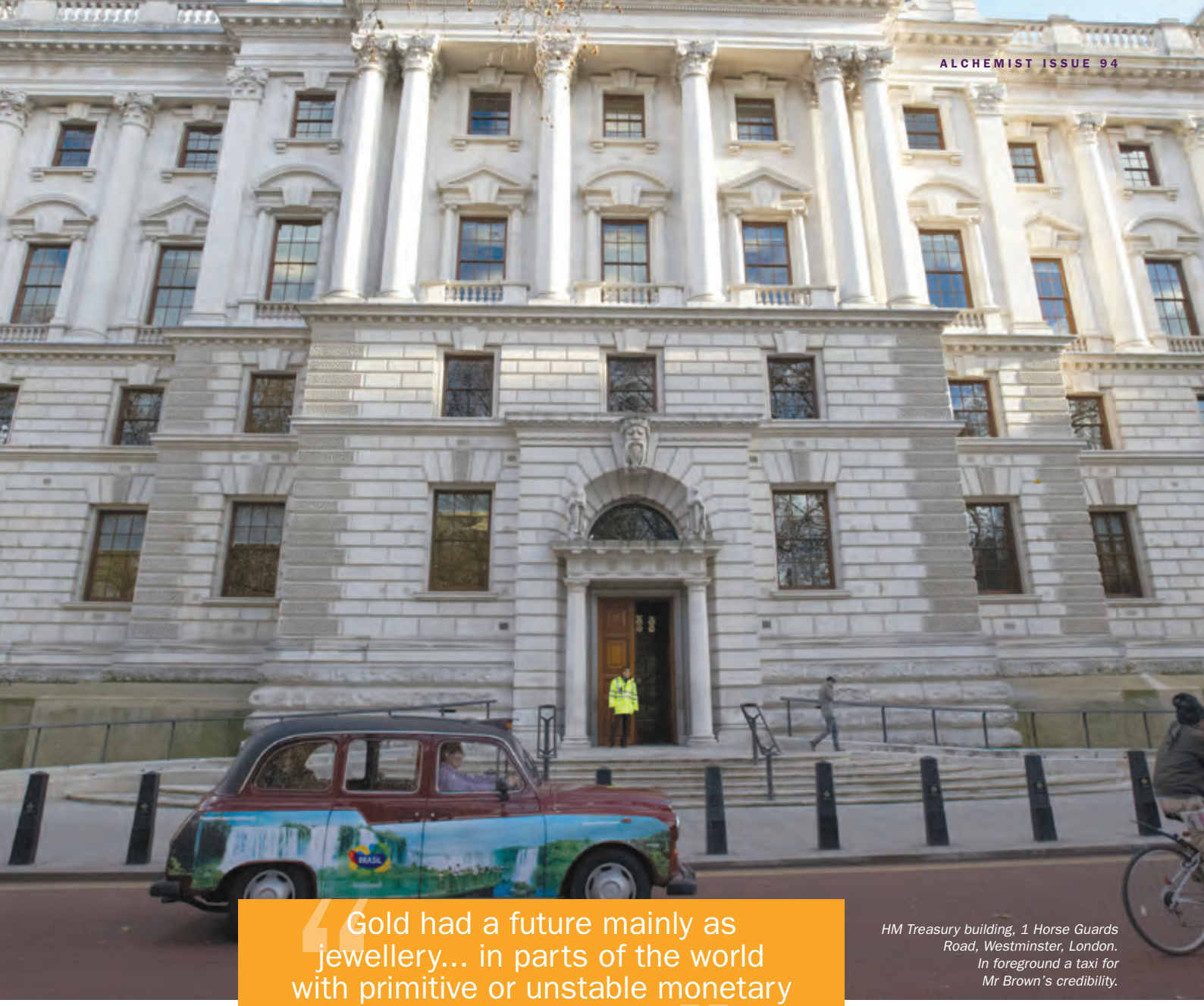
Announced at that September's annual IMF (and with Switzerland and the BoE among its 15 signatories), this sudden transparency so clearly reassured the market that the next morning gold made its sharpest one-day jump since 1982, starting a two-week gain of 25% that hasn't been beaten since.

FIGURE 2: ALL THE GOLD ABOVE GROUND



Value as percentage of world GDP
Percentage in official-sector control

Source: BullionVault via Timothy Green, Metals Focus, various



HM Treasury building, 1 Horse Guards Road, Westminster, London. In foreground a taxi for Mr Brown's credibility.

> "Gold had a future mainly as jewellery... in parts of the world with primitive or unstable monetary and financial systems"

Renewed three times, a fifth Central Bank Gold Agreement shouldn't waste much time this September when the current deal expires, because any sales cap became redundant when Western selling ended amid the global financial crisis in 2009 (Figure 1). So too did any pretence of wanting to defend Western currency values or needing reserve assets to do so, replaced by bail-outs, QE money creation and near-zero to negative interest rates. Together, this has revived a strongly symbolic role for gold among the public (shown by grass-roots campaigns to "Bring home our gold!"). It has also seen a surge in emerging market nations buying gold to hedge those Western reserve currencies under attack from their own issuers.

A MISSED OPPORTUNITY

Led by Russia, China and Turkey, 30 different countries have added to their gold reserves over the last decade, of which only two are what we now call 'Western' nations (Poland and Hungary recently doubled and raised gold ten-fold repectively, but only to 10% and 4% of foreign reserves; their European Union partners average is 26%) and only one is classed as an advanced economy (South Korea). More crucially for our market, however, the "elusive investor" who GFMS's Timothy Green noted was missing throughout the 1990s has returned in force.

Coins, bars and exchange-traded trust funds backed by bullion have accounted for nearly one-third of global demand so far this decade, up from an average 19% in 2000-2009 and barely 10% in the late 1990s.

Longer term, this means that while central banking's switch to net buying has slowed the reprivatisation of gold now running since the collapse of the post-WWII Bretton Woods system, it has not yet reversed it. Official sector holdings in 1968 accounted for some 40% of all the gold ever mined in history. By 1999, that figure had fallen below 25% and it is now flattening (but still falling) at around 17% (see figure 2).

"If properly marketed, these [auctions] could act as a shop window for gold," wrote the BoE's Smout here in *The Alchemist* after the UK's 1999 announcement. Peter Fava, then chair of LBMA, also thought selling Treasury gold direct to the public would "be a great opportunity", and perhaps it could have soothed tabloid anger, because "the money raised by privatisation, while useful, has always been a second-order question", as Brown's predecessor Nigel Lawson said of the 1980s' hugely under-priced sales of state assets such as British Gas, British Telecom and council housing under Margaret Thatcher. But New Labour couldn't possibly promote the barbarous relic as a wise investment, not when Brown's economic management meant *Things Can Only Get Better* as the party kept promising by taking D:Ream's chart-topper for its conference anthem.

GOLD AND HISTORY RETURN

Alongside central banking and PR spin-doctoring, geopolitics also seemed to be nearing perfection as the 20th century drew to a close, or so Western policymakers thought after skim-reading the back of US State Department Director Francis Fukuyama's best-selling *The End of History*. The book was more nuanced than the jacket blurb, but Soviet Communism's collapse, plus China's move towards a market-based economy (albeit run by a military dictatorship), appeared to confirm that the world had "no alternative" to Anglo-American capitalism, resulting in the "end state of the historical process ... a moment in which a final, rational form of society and state became victorious".

Put into more practical terms for reserve managers, "The traditional reasons for holding gold have included the war chest argument", as the UK Treasury said in its 7 May 1999 press release. But who needed a war chest when our side kept winning? That very night, the US Air Force bombed the Chinese Embassy in Belgrade, killing three people, thanks to a failure of CIA intelligence in NATO's "humanitarian intervention" against Serbia over its policy in Kosovo.

THE CBGA'S SALES CAP BECAME REDUNDANT WHEN WESTERN SELLING ENDED AMID THE GLOBAL FINANCIAL CRISIS. SO TOO DID ANY PRETENCE OF WANTING TO DEFEND WESTERN CURRENCY VALUES.

Adrian Ash was previously managing editor of tech-stock tipsheets and the pro-gold *Fleet Street Letter* in the early 2000s. He now is Director of Research at BullionVault, the physical gold market for private investors online first developed because, with Gordon Brown dumping gold, it must deserve proper investigation.

For investors at least, "Gold remains the cleanest insurance against such overconfidence", as SocGen analyst Dylan Grice noted 10 years after the Brown Bottom. Skip forward another 10 years, and US stock markets are again testing new all-time highs as investors pour cash into unproven ideas (83% of new US listings were loss-making companies in 2018, beating even the tech bubble's 2000 peak). As for politics, "the liberal idea is obsolete", declared President Putin of Russia, gold's heaviest nation-state buyer since the Brown Bottom, at June's G20 meeting in Osaka, Japan. With gold's no.2 buyer, China, also boldly challenging Western hegemony around the globe, the turmoil of the past 20 years suggests it's not worth trying to forecast how gold's role will adapt to the next 20 years of financial and political change.

But if gold does continue to grow its value and use among reserve assets, the Treasury's decision of 1999 will mean the UK starts the future very much in the second rank.

> "For investors at least, Gold remains **THE CLEANEST INSURANCE** against such overconfidence"

ASM SOURCING: The Risks & Rewards – a DRC Case Study

BY MATTHEW CHAMBERS, CHAIRMAN, CHAMBERS FEDERATION

THE DEMOCRATIC REPUBLIC OF CONGO

For more than a century, the Democratic Republic of the Congo (DRC) has been plagued by regional conflict and a deadly scramble for its estimated $24 trillion wealth of untapped minerals[1]. Profit from the mineral trade is one of the primary motives for the conflict – the deadliest since World War II. The UN Group of Experts on the DRC estimates that 98 percent of the artisanal and small-scale mine (ASM) gold produced is smuggled out of the country[2], which in turn fuels conflict and deprives the population of significant revenues and benefits, and undermines the stability of the region – a vicious circle.

Over the past decade, several government development programmes, such as USAID, have invested countless millions, working in partnership with the DRC government, in building responsible ASM supply chains. DRC has been a testing ground for a variety of responsible sourcing initiatives, which started early with successes in the 3Ts, yet lagged behind in the gold sector. The environment in DRC provides a vetting through 'survival of the fittest'. It is an environment of diverse extremes, so that if success can be achieved here, it can be replicated and achieved anywhere in the world. Each programme developed its own unique approach, but little collaboration existed and, until recently, best practices were largely lost once donor funding for a programme ended. Starting with the first exports of responsible gold in the beginning of 2018, the Fair Congo Initiatives was founded as a social enterprise, with assistance from USAID, to be that 'missing link' between the work of development programmes on the ground in eastern DRC and markets in the US, Canada and Europe. Working through groups such as the Responsible Artisanal Gold Solutions (RAGS) forum, private sector actors such as Asahi, Richline, Signet and Fair Congo were able to combine these best practices together and bring to market the first responsible gold from DRC to the US market. Working in collaboration with and aggregating responsibly sourced and fully traced ASM gold from every programme in the country, including Bundesanstalt Fur Geowissenschaften und Rohstoffe (BGR), IMPACT, Peace Direct and the USAID-funded Responsible Mineral Trade (RMT), Fair Congo continues to bring to market ready-to-scale supplies of responsible gold to the US, Canadian and European markets.

THERE ARE MORE THAN 1,700 ASM GOLD SITES IN EASTERN DRC, RANGING IN SIZE FROM LESS THAN 10 MINERS TO SEVERAL THOUSAND

SCALE AND DEMAND WORLDWIDE

There are more than 1,700 ASM gold sites in eastern DRC, ranging in size from less than 10 miners to several thousand[3]. An estimated 11.6 tonnes are produced annually, with each artisanal miner producing approximately 1.17g per week and generating approximately $437 million per year for the local economy[4]. These figures, in addition to the 30 tonnes of LSM gold produced annually, place the DRC firmly as one of the most important African gold producers.

In 2018 alone, there was well over half a ton of Fairmined and Fairtrade gold exports brought to market across the globe, yet these organisations estimate the demand to far exceed 2 tons. As the current demand outstrips the supply and the demand continues to grow, this creates opportunity for progressive downstream actors to fill that demand. As responsible sourcing programmes expand and enter new producing countries, progressive actors should work early to build these new sourcing relationships to secure diversity to their supply as worldwide LSM gold supplies reduce[5].

1. UN News, https://news.un.org/en/story/2011/10/390912-dr-congo-un-advises-prudent-use-abundant-resources-spur-development, 10 October 2011. **2.** Bafilemba, Fidel and Sasha Lezhnev, "Congo's Conflict Gold Rush: Bringing gold into the legal trade in the Democratic Republic of Congo," The Enough Project (April 2015.) **3.** Analysis of the interactive map of artisanal mining areas in eastern DR Congo; 2015 Update available at: http://ipisresearch.be/wp-content/uploads/2016/10/Mapping-minerals-in-eastern-DR-Congo_v005.pdf: accessed 18 June 2019. **4.** Ibid, pg. 16 – accessed 18 June 2019. **5.** www.bloomberg.com, *Decade of Gold Mine Declines Poised to Spur Deals, Price*, by David Stringer, 15 November 2016.

MANAGING EXPECTATIONS

Accessing economies of scale is possible in the DRC; however, this requires an understanding of the realities faced by small-holder miners and co-operatives. Limited and outdated infrastructure and overworked local governing bodies can lead to slower-than-expected export times and costs. Changes in weather, delays in banking transactions and even local political elections can create a disconnect in the understood realities if you've never lived and worked in a developing economy. Starting to source ASM gold is also a long-term relationship, something that needs maintenance and consistency. Disruptions in cashflow and inconsistent sourcing are not compatible with the survivability of ASM communities who depend on reliable commercial partners. It's also important that any refining partner has the capacity to segregate and process in small batches.

RISKS AND MITIGATIONS

Due Diligence and Traceability

After Dodd-Frank was passed, many industry schemes, responding to section 1502, failed to value the existing systems and technical competencies and capacities of the ASM community in an attempt to replace, not strengthen, what had been an operational, if informal, artisanal sector and reactionary economic landscape. This top-down approach doesn't have the sustainability that more organic methods, such as the CRAFT Code does. While creating sustainable self-reliance, it was important that Fair Congo recognised the importance of local experience, learning lessons about how to integrate knowledge and respect for traditional culture, and its integration in the formal economy.

As the first commercial operator to implement OECD DDG in the region, Fair Congo continues to develop and implement a grass-roots framework which can contribute to a viable pathway for co-operatives to responsibly bring their gold to market at scale. Frameworks such as these create a constructive environment where artisanal producers can implement effective due diligence specific to their operating environment and work towards continuous improvement.

Cash Flow

Artisanal sourcing often requires some level of advanced payment, especially in areas like the DRC where the informal capital markets can be well established, although, financial management capacities in the upstream ASM supply chain can often be limited.

As inventory is rarely held by producers, it is key that the aggregator, whether a financially stable co-operative or exporter, has a consistent and reliable cash flow to purchase ASM gold as it is produced. Even though well-established informal capital is locally available, it isn't consistently available and is often managed by very untrustworthy people, which provides an opportunity for well-funded formal aggregators to replace the informal ones through reliability. Additionally, by using the formal banking system and keeping financial transactions as cashless as possible, it allows the traceability of payments further upstream more than ever before. Fair Congo takes it even further by aggregating all advanced payments in the US and is implementing a mobile money platform into its sourcing sites.

REWARDS

Sourcing Portfolio Diversification

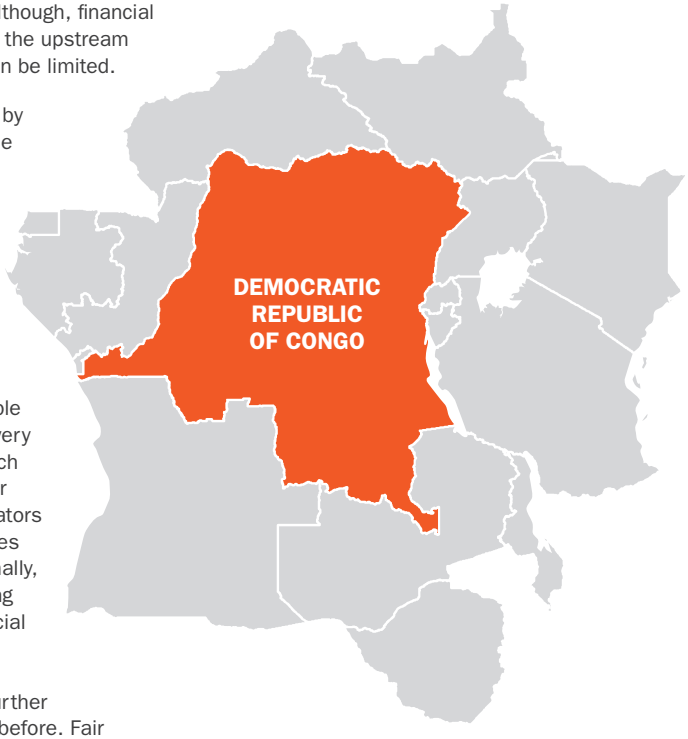
Artisanal gold production is never consistent as it ebbs and flows for a variety of reasons from weather to available manpower. Just as with investing, it's important to diversify to hedge risk. It's inevitable that as LSM production capacity decreases, gold values are likely to increase due to scarcity, which in turn will incentivise more rural workers to enter into the ASM space. This combination of factors has the potential to increase the global 'primary' production input from ASM from its current estimated 20%[6] to even greater numbers. As artisanal sites vary in size and capacity, having a diverse group of artisanal sites mitigates the disruptions in inventory flows and spreads the risks from potential regional instability.

Progressive Industry Lead

As seen throughout different industries, those who take greater risks and take the lead with progressive, socially focused business models often increase their market share to become industry leaders in the long term. While risks from sourcing ASM gold can be high relative to LSM, the rewards can far outweigh those risks if the actors implement the appropriate risk management approaches.

CSR, No Longer Just Philanthropy

While having a CSR budget is an important line item to maintain, there are other ways to enhance a corporation's positive social impact without adding cost.



6. Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development (IGF), Global Trends in Artisanal and Small-Scale Mining (ASM): A review of Key numbers and issues, https://www.iisd.org/sites/default/files/publications/igf-asm-global-trends.pdf

By sourcing responsibly from ASM, companies can meet the public's, and their shareholders', demands for social responsibility while adding little to nothing to their operating costs. This, in turn, allows ASM actors to professionalise and access markets that pay consistently and responsibly. As they do, they are able to reinvest in organisational management and address more fundamental challenges in a way that fits international market standards and regulations.

INNOVATIONS

Alternative Livelihoods = Opportunity for Progressive Marketing

Owing to the rural overlap of artisanal mines and agro-economic production zones, Fair Congo's close relationship with small holder producers (more than 25,000 miners and farmers) also presents opportunities for the population to diversify their livelihoods between ASM and agricultural business, and strengthen their household income portfolio. Fair Congo has launched a fine cocoa, single-source, organic and traceable bean-to-bar chocolate company, managed and produced entirely by women, which operates successfully in parallel with traceable artisanal gold exports. The producers and consumers along the gold and cocoa value chains are similar. The producers upstream overlap geo-demographically, and the finished products are targeted at the same consumer base downstream – those concerned with ethical sourcing, a growing consumer demographic.

New Financial Instruments

Already aggregating all exports and downstream finance within the US, Fair Congo's success demonstrates its expertise in context-specific risk management. All payments are received and managed by its parent company based in the US, which is now launching the first US bond focused on CAHRAs, which will be used in part to facilitate secured inventory financing for responsible gold sourcing, mitigating risk for buyers and securing upstream supply contracts.

SCALE AND COUNTRY EXPANSION

Artisanal export relies on a context-specific understanding and adaptable business strategy. Since successfully implementing the first pilot exports, Fair Congo is now scaling up activities to increase its supply coverage of mine sites and partnerships both within DRC and through expansion to other ASM gold-producing countries.

journeyofgold.org

To highlight the importance and benefits of responsible sourcing, Google teamed up with the Responsible Artisinal Gold Solutions Forum and StoryUp XR to create Journey of Gold, available on YouTube.

The film offers a glimpse into the lives and conditions of those working at a low tech, small scale mine in Nyamurhale – one of just three conflict-free artisinal gold mines in the DRC.

Matthew Chambers is a US accredited impact investor who founded the Chambers Federation, a leader in building inclusive and sustainable business in CAHRAs. Nominated for the 2019 USDoS Ace Award in corporate excellence in sustainability and women empowerment, Matthew draws on experience in founding previous enterprises including a financial services company which managed over $2.5 billion in government and bank assets during the 2008 financial crisis. He also founded a woman owned and operated construction company in Kenya which built the first entirely woman-built road in the country. He co-founded the Fair Congo Initiatives in 2017 with his wife Adele Gwet who is the managing director, formerly with the United Nations and African Union.

Now living in eastern Congo, they invest into the development of responsible supply chains of gold, chocolate and coffee and take exporting and aggregation further into the development of local value addition. In less than one year, their initiative has created the first supply chain of responsible ASM gold from a CAHRA into the United States as well as the first premium chocolate production facility in the country, run entirely by women. As the initiative grows, the addition of gold jewellery and component production, again made by women, is the newest development.

For more information on sourcing responsible ASM gold please email **matthew@chambersfederation.com**

LBMA NEWS

2019 AGM

LBMA's 31st Annual General Meeting took place at Glaziers Hall on 11 July. Details of the subcommittee and Chairman's reports are available from our new portal, MyLBMA (see page 17 for details).

Annual Review 2019 LAUNCHED

The Review sets out the work that we have been doing over the last 12 months. In particular we are excited by the liquidity analysis on the new trade reporting data, which we have done, which shows that gold stacks up impressively compared to other asset classes classified as Extremely High Quality Liquid assets.

LBMA has also continued its work on ensuring integrity for the market with the expansion of its Responsible Sourcing Guidance to include Environmental, Social and Governance (ESG) issues.

As the conference heads to Shenzhen in October, LBMA has also increased its global engagement in Asia through, LBMA Asia. Broader industry engagement is crucial to LBMA's success in fulfilling its mission to represent the interests of the global precious metals industry.

We held a Press Conference on the morning of the AGM to promote these key findings which was well received. You can find the Annual Review on our website but if you would like a hard copy please contact **mail@lbma.org.uk**

LBMA-i TRADE REPORTING

At the end of June, as the gold price hit a six-year high, the weekly total gold trading volumes for the week also hit a record high, with in excess of 227 mn oz ounces traded. This compares to the overall weekly average since November of 151 mn oz ounces and the latest 12-week moving average of 160.1 mn oz ounces.

On 1 July, daily data for platinum and palladium were added to the suite of datasets that LBMA-i now offers subscribers.

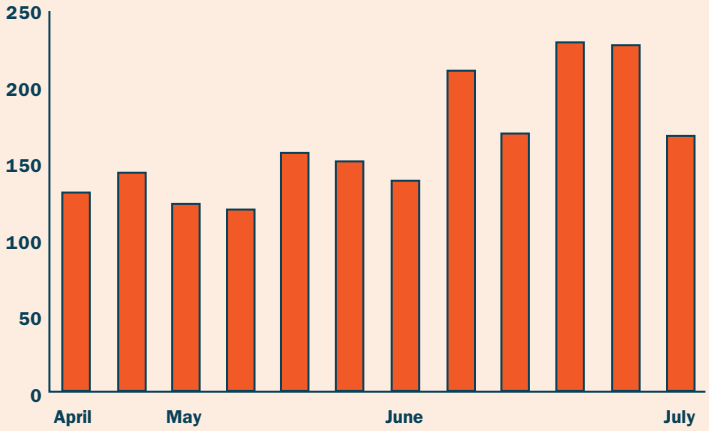
The LBMA-i service is provided by LBMA and Nasdaq, following the acquisition earlier this year by Nasdaq of Cinnober A.B. and its subsidiary, Simplitium Ltd.

WHY THE DATA IS IMPORTANT

LBMA-i market data makes it possible for market participants to gauge the size, shape and liquidity of the OTC market as represented by LBMA members.

It also helps support LBMA's dialogue with regulators on such matters as NSFR, where we are working closely with key stakeholders to gain a full exemption for precious metals and clearing.

GOLD TOTAL WEEKLY VOLUME (MNS OUNCES)



The chart shows the total weekly volume of gold trade reporting data for the period from 15 April to 7 July 2019

Susannah McLaren joins LBMA

LBMA is delighted to welcome Susannah to the team as LBMA's new Compliance and Responsible Sourcing Manager. She manages LBMA's Responsible Sourcing Programme for precious metals, which is mandatory for all LBMA Good Delivery List Refiners.

She is an expert in human rights and broader sustainability, with over 15 years' in-house and consultancy experience in the field. As we welcome Susannah, LBMA would like to thank Simon Houghton-Dodd, who she has replaced, for all his hard work and wish him all the best for the future.

MyLBMA IS NOW LIVE!

MyLBMA is our new digital portal and will provide all of our stakeholders with a centralised touchpoint to engage with LBMA, along with a range of tailored content for members and Associates, as well as the ability to manage their unique user account.

We have not forgotten non-members either as the portal offers everyone the opportunity to register and set up an account.

We are particularly excited to report that both our membership and our GDL applications can now be accessed in MyLBMA, thereby streamlining the application process.

MyLBMA will continue to evolve, and we welcome feedback on the existing content as well suggestions for how we can enhance it in the future.

MyLBMA FEATURES INCLUDE:

Secure online access Committee members can access papers and minutes securely.

An easy and convenient way to manage your LBMA subscription preferences, including receipt of our key publications and ability to update your contact details and profile.

Tailored content to reflect membership type, including news updates, regulatory briefings, upcoming events, as well as the ability to download branding guidelines and member/refiner logos.

Web-based applications for membership and Good Delivery accreditation.

View any invoices from LBMA relating to subscriptions or registration for our events.

FOR YOUR UNIQUE REGISTRATION LINK TO THE PORTAL, PLEASE EMAIL emmy.richardson@lbma.org.uk

JOIN THE LBMA PRICE AUCTIONS

The gold price celebrates its 100th birthday this year and we have a number of events planned in 2019 to mark the occasion – see page 7 for details. Back in 1919, there were just five participants in the auction, but since IBA became the independent administrator in 2015, the number has trebled to 15 participants (and 12 for silver).

As we look to the next 100 years of the gold price, LBMA would encourage any interested members or Associates to join the auctions, using the contact details below.

- Gold or silver price auctions, ICE Benchmark Administration: IBA@theice.com or +44 (0)20 7429 7100, or
- Platinum and palladium auctions, LME: market.access@lme.com or +44 (0)20 7113 8888.

102 ACCREDITED REFINERS

We now have **102 refiners** on the Good Delivery Lists, with **67** listed for gold, **83** listed for silver and **48** refiners on both lists.

67 GOLD

83 SILVER

CURRENT APPLICATIONS

There are currently 6 active Good Delivery applications.

GOLD AND SILVER Held in London Vaults

As at the end of March 2019, there were **7,671** tonnes of **GOLD**, valued at **$319.5** billion, and **36,195** tonnes of silver, valued at **$17.6** billion. This equates to approximately **613,696** gold bars and **1,206,499** silver bars.

LBMA MEMBERS

We currently have 143 member companies – 87 Full Members (including 12 Market-Making Members and 12 Affiliates), 3 Exchange Affiliates and 53 Associates.

LBMA OUTREACH

The LBMA Executive has participated at a number of industry events recently, a selection of which are highlighted below.

Recent Event Summary

9-11 June, SBMA Asia Pacific Precious Metals Conference, ParkRoyal, Singapore Sakhila Mirza delivered a presentation about the extent to which regulation is impacting on the precious metals market.

15-18 June, IPMI 43rd Annual Conference, Reno, Nevada, USA Neil Harby and Ed Blight attended the event, as part of our continued outreach. Neil delivered a presentation explaining the latest LBMA initiatives and developments in the global OTC market.

26-28 June, Forum on Central Bank Foreign Currency Operations, Pretoria, South Africa As part of LBMA's drive to engage closely with the central banking community, Neil spoke at the event explaining LBMA's central role in the global OTC precious metals market.

8 July, OECD-Borsa Istanbul Joint Training Workshop, Istanbul The workshop was focused on the OECD Guidance on Responsible Supply Chains of Minerals from Conflict Affected and High-Risk Areas. Sakhila's presentation was aimed at raising awareness on due diligence and how LBMA are leading the industry with its mandatory Responsible Sourcing Programme.

UPCOMING INDUSTRY EVENTS

FROM 22 JULY:
325 years of the Bank of England Exhibition

Bank of England Museum,
Bartholomew Lane, London EC2R 8AH

27 July 2019 marked the 325th anniversary of the Bank of England. To commemorate the occasion the Bank has arranged a new exhibition, 325 years, 325 objects.

The exhibition highlights key developments in the Bank's role and remit, but the main focus is on the place and the people rather than the technical work of the Bank. Key themes include life at the Bank, representation and inclusion. The 325 objects have been carefully selected from the Bank's own collection of 50,000 objects. It is a must see exhibition.

09-13 SEPTEMBER:
LPPM Platinum Week

New York, USA

12 SEPTEMBER:
LPPM Cocktail Reception

The Lotte New York Palace Hotel,
455 Madison Avenue, New York

The London Platinum and Palladium Market, together with LBMA, is holding a Cocktail Reception for its members on Thursday, the from 18:00-20:00. **This is an invitation only event.**

The cocktail reception is followed by the IPMI Dinner at the same venue. The Guest speaker is Ed Coyne of Sprott Money Management. **This is an invitation only event.**

15-18 SEPTEMBER:
30th Denver Gold Americas Forum

Hyatt Regency, Colorado, USA

Keynote speakers at the event are Pierre Lassonde (Franco Nevada), Douglas Silver (Orion Mine Finance) and Suki Cooper (Standard Chartered).

02-03 OCTOBER:
Joburg Indaba

Inanda Club,
Sandton, South Africa

28-31 OCTOBER:
LME Week

London, UK

18-19 NOVEMBER:
IPMI Europe Chapter Seminar

Lisbon, Portugal

The Seminar focuses on Precious Metals Products and Technologies.

GENTEEL FAIR PLAY: THE CULTURE OF THE LONDON GOLD MARKET

BY RACHEL M. HARVEY, PHD, ADJUNCT ASSOCIATE RESEARCH SCHOLAR WITH THE CENTER ON GLOBAL ECONOMIC GOVERNANCE, COLUMBIA UNIVERSITY

"If you're interested in global finance, why not instead study the larger credit default swaps market?" It was a fair question from an individual I was interviewing. I responded by explaining how Timothy Green's research (Green 1993) on the world gold market had captured my attention.

It was early 2006 and I was in London researching how the London gold market's culture has shaped its development throughout the 20th century. If I had been asked the same question after the 2008 global financial crisis, I would have responded differently. In the aftermath, scholarly and policy analyses identified flawed incentive structures (the rewards and sanctions governing market behaviour) as important factors contributing to the predatory lending, excessive risk-taking, regulatory arbitrage and other questionable practices underlying the crisis. Reflecting on my data, I realised that if the markets at the centre of the debacle had a culture similar to that of the London gold market – with its emphasis on participants having a collective responsibility toward fostering the long-term health of the market – then several factors underlying the crisis would have been counteracted.

I REALISED THAT IF THE MARKETS AT THE CENTRE OF THE DEBACLE HAD A CULTURE SIMILAR TO THAT OF THE LONDON GOLD MARKET THEN SEVERAL FACTORS UNDERLYING THE CRISIS WOULD HAVE BEEN COUNTERACTED

THE 'GENTEEL FAIR PLAY' CULTURE

The data I gathered revealed the existence of a 'genteel fair play' culture[1] in the London gold market (LGM). While it appeared to shape the market as early as the 1930s, the most robust evidence of its existence is from the 1970s. Traders recalled bullying each other, competing aggressively and trying to "kill each other with a smile". They also recounted a parallel system of conduct characterised by co-operation, honourable forbearance and an overarching duty to create a healthy and sustainable market. In this manner, the values of loyalty, duty and honour underpinned the functioning and regulation of the LGM.

Honour was essential to gold dealing and market settlement. Once a trader quoted a price, they could not alter the figure even if the quoted price meant they would lose money. Gold traders were expected to quote a reasonable spread, or difference, between their buy and sell prices. These practices were critical for creating market liquidity. The reliance upon a counterparty's honour was particularly important since settlement was handled informally. Usually, each trade was scribbled into a dealing book or recorded on a trading slip. During hectic periods, however, trades could get lost in the shuffle. If unmatched sales or purchases emerged during settlement at the day's end, then the transaction would be split among the parties – regardless of whether it resulted in a profit or loss for them. Reputation and honour were also the basis of credit control. Well into the late 1970s, a majority of the bullion firms were owned by thinly capitalised merchant banks (when compared to American, German and Japanese financial conglomerates). Trust was placed in the firm that it would honour the obligations of its traders – even if it meant that the firm took a large loss[2].

1. This normative order was a subculture of the chivalric ideal of gentlemanly conduct institutionalized in the late-nineteenth and early-twentieth institutions of the British elite. The presence of a modified version of this ethos was grounded in the socialization of the bullion firms' owners and managers; the organizational structure of the bullion firms; and the small, dense social networks characterizing the LGM (Harvey 2015). **2.** Multiple interviews, London, 2006 and 2007.

The culture also shaped how the Bank of England (the Bank) regulated the LGM. Instead of utilising legislation, it preferred an informal governance style that emphasised the values of loyalty, duty and honour. The Bank expected its employees and the firms it regulated to do what they said they would do (Courtney and Thompson 1996). While rule violators faced expulsion from the financial world, the Bank appeared to effectively halt any problematic behaviour with a phone call or a rule violator visiting its premises for a quiet discussion.

Individuals acted according to the genteel fair play ethos for reasons that went beyond the strategic, rational cost-benefit calculating behaviour normally associated with markets. This is seen in the use of numerous gentleman's agreements between the dealing firms to limit competitive behaviour (e.g. fixing commissions, discouraging the poaching of another firm's clients)[3]. Clearly, these arrangements protected the pecuniary interest of the bullion trading firms, but they were also based in a collective responsibility towards fostering stable market making. Competition was valued, but it was seen to have limits. As one individual noted, the market should never be "bled for the margins" or fall prey to ruinous rivalry[4].

A similar dynamic was seen in the boundaries placed on earning profits from transactions. Several interviewees who traded gold in the 1970s noted that they would not make money on a position if it was based on an unfair advantage. One trader told me about a scenario in which he had an opportunity to profit off another dealer who recorded their transaction incorrectly. This individual explained that the right course of action was to correct the counterparty's mistake. If he did not do this, the person would never trust him in future. At the same time, he also noted that if you acted in a dishonourable way, then you were just that – dishonourable.

HONOUR WAS ESSENTIAL TO GOLD DEALING AND MARKET SETTLEMENT

A similar approach to profit-making was seen in client dealings. Traders could have profited at the expense of clients by colluding, e.g. demonstrating honour among thieves. Yet, evidence suggests that such behaviour was frowned upon. For instance, in the 1970s, price movements ceased when the LGM closed for the day. The practice was to telegraph clients in Europe asking whether there was any interest in buying or selling gold at the closing price. The next morning, telegrams from Europe would be waiting. Once, a client's telegram was delayed, during which time the price had moved upwards.

Instead of making the sale at the new price, the firm transacted the deal at the previous day's closing price. Doing otherwise would have been seen as making money from an unfair advantage. Summarising his experiences in the LGM, one trader noted that he had just "tried to do the honourable thing"[4].

The Bank's commitment to this ethos also went beyond strategic concerns. In the 1930s, for instance, the Bank made efforts to control speculative currency and gold transactions. Instead of utilising legislation, Bank staff circulated a letter explaining the guidelines to be followed. While they pondered legislation, they instead decided to rely upon the "loyalty and discretion of the market" to curtail speculative transactions (see panel 1). The non-strategic commitment to this regulatory approach still existed in the 1970s (see panel 2). The Bank was the "moral authority of last resort" for the genteel fair play ethos.

GENTEEL FAIR PLAY AFTER THE 1970s

After the 1970s, the cultural and institutional infrastructure supporting market-making in the LGM changed. With the repeal of exchange controls in 1979, skyrocketing gold prices and high inflation, participation in the market grew dramatically. By 1985, the market had expanded from five to more than 55 firms. The small intimate environment dominated by the genteel fair play culture gave way to a larger market with a more aggressive trading ethos. The poaching of clients (and employees) became regular practice. Fixed commissions and spreads went by the wayside. Over time, companies also became more reluctant to allow employees to volunteer in market infrastructure 'maintenance' activities.

Countering these trends in the 1980s was a cohort of traders who entered the LGM between the late 1960s and the mid-1970s. These individuals became the primary bearers of a modified genteel ethos which emphasised a custodial commitment toward creating a healthy and sustainable market. Many of these traders spearheaded the creation of London Bullion Market Association (LBMA). They guided the new organisation to formalise many existing market practices and develop rules that, at the very least, implicitly embodied elements of the older ethos.

Becoming an LBMA member, for instance, involved a temporal and monetary commitment to the LGM. Applicants needed to have at least a year-long, bullion-based trading relationship with at least three LBMA members prior to applying for membership.

3. These were in addition to the state-mandated exchange controls that placed restrictions on who could trade in the wholesale gold markets until 1979. **4.** Interview, London, 2006.

The legacy of the genteel ethos also informed the differentiated trading commitments of the membership levels. The highest market-making membership level required a company to possess the relevant personnel and infrastructure to quote continuous two-way prices on a full range of gold and silver products. Other marking-making members needed to be active traders in both gold and silver. This ethos was also reinforced by the sense of community LBMA cultivated among members with its voluntary committees, annual conferences, dinners and workshops. Even in the face of changing market conditions since the 1970s, LBMA and a core cohort of traders have preserved elements of the genteel fair play ethos in the LGM's governance.

MANY OF THESE TRADERS SPEARHEADED THE CREATION OF LBMA

LESSONS FROM THE PAST

In light of contemporary electronic markets, the genteel fair play ethos might seem quaint, if not antiquated. Yet, it yields at least two lessons for today. First, the culture was prevalent throughout the LGM and its institutions. It informed relations between traders, the bullion firms and the Bank. Regardless of whether commitment to the ethos was based on strategic or non-strategic motivations, its multilayered enforcement made it the generally accepted way to conduct business.

THE CULTURE ALSO SHAPED HOW THE BANK OF ENGLAND (THE BANK) REGULATED THE LGM

Second, while the LGM's ethos might seem perfectly 'old fashioned'", elements of its culture are often presumed to be critical for successful market regulation and sustainable market-marking. Markets are characterised by uncertainty, information asymmetries and imperfect monitoring. To be fully effective, incentive systems must have continuous monitoring mechanisms or leave participants with the sense of constant surveillance. Unless these conditions are met, incentive systems will risk failing because it is impossible to watch everyone all of the time. Opportunistic behaviour and malfeasance will eventually emerge. Compliance with market governance thus works best with a culture similar to the genteel fair play ethos.

PANEL 1

Text of a Bank of England archival document

THEORY

Hoarding: means everybody his own banker. Is contagious and spreads panic. Arises out of, and contributes to the discredit of all those who deal in and depend upon credit.

ETHICS

Fancy prices approximate to a swindle. London has everything to gain by being Caesar's wife. Banking is not money-changing, c.f. buying sugar by the cwt. in a general strike. Taking advantage of those who know no better: and spreading the pestilence by house-to-house calls, etc. Premium justified when for the sake of centralising gold: but dealing the other way profits nobody but the middle man. On balance the customer loses. Panicky quotations disturb and disorganize currency markets and are certainly our legitimate concern.

ACTION TAKEN

Switzerland and Holland: B.I.S. [Bank of International Settlements] circular letter (extract below). Only principles asserted, their application left to the loyalty and discretion of the market.

ATTITUDE OF THE MARKET

Is it general? Nonsense to talk of legislation ad hoc. But do they mean they would prefer administrative, departmental action, or by-laws? This would certainly be with the trend of the times. But we prefer guidance, which relies and depends upon loyalty: not blind loyalty, but at the same time not malicious or subversive criticism.

Source: Memo authored by Harry A. Siepmann, June 19, 1936, Bank of England Archives, C43/199/177

PANEL 2

Excerpt of a Federal Reserve Bank of New York archival document

This morning I called Mr. R.D. Galpin, Deputy Chief Cashier, Bank of England, to discuss Bank of England's letter concerning guarantees by parent banks located outside the United Kingdom of their banking consortia and other subsidiaries in the United Kingdom... Mr. Galpin explained that in seeking guarantees from parents abroad the Bank of England was not requesting legal document, but rather a "moral obligation." This obligation would express the desire and intention of the shareholders to assure their pro rata share of the liquidity of their subsidiary in the United Kingdom. This moral obligation was undertaken orally before each of the subsidiaries began operations in the United Kingdom. The written expression is taking either of the two forms – as resolution of the consortiums bank's board of directors or letters from the consortium bank's shareholders.

Memo of telephone conversation between Willey, Federal Reserve Bank of New York, and Galpin, Bank of England, October 25, 1974

Source: Federal Reserve Bank of New York Archives, C261 – England, Bank of England, 1974.

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Rachel M. Harvey, PhD is an Adjunct Associate Research Scholar with the Center on Global Economic Governance, Columbia University. She received her PhD in sociology from the University of Chicago. She is a Fellow with the *Framing the Global Research and Publication Project*, Indiana University. Her publications include *Money, Markets, and Struggles against the State: Reframing the Global and the Particular* (forthcoming, Indiana University Press) and "The Legal Construction of the Global Foreign Exchange Market" (2013, Journal of Comparative Economics).

IS GOLD THE ULTIMATE RECESSION HEDGE?

BY RONALD-PETER STOEFERLE, MANAGING PARTNER, INCREMENTUM

In Q4 2018, stock investors were brutally reminded that volatility could in fact experience sudden and unexpected surges. Emerging growth worries as well as concerns about the sustainability of the fiscal situation have re-entered the discourse among market participants. Former Federal Reserve chair Janet Yellen has even taken back her infamous statement that she did not expect a new financial crisis in her lifetime and now sees "gigantic holes in the system"[1,2]

Times have changed in the 10th year of economic boom. While no new financial crisis may be looming on the horizon yet, economic expectations have continuously deteriorated in recent months[3]. It appears that signals of a US recession are slowly increasing.

INVESTORS ARE LOOKING FOR SAFE HAVENS IN TIMES OF CRISIS, AND GOLD IS THE CLASSICAL SAFE-HAVEN ASSET

The Federal Reserve's recession indicator currently indicates a recession probability of 27.5% for April 2020[4]. In the past 30 years, whenever this figure has been so high a recession set in during the following two months. Moreover, the yield curve – which has the best track record for recession forecasts – also clearly confirms that the recession clouds on the horizon are getting darker.

27.5%

THE FEDERAL RESERVE'S RECESSION INDICATOR CURRENTLY INDICATES A RECESSION PROBABILITY OF 27.5% FOR APRIL 2020[4]

BUT WHAT WILL HAPPEN THIS TIME AS CLOUDS GATHER ON THE ECONOMIC HORIZON?

The two most recent recessions (2000 and 2008) led the Fed to cut its interest rates by 500 basis point[5]. At the moment, the Fed funds rate stands at 2.25%-2.50%. The potential for interest rate cuts thus appears to be severely limited, unless one were to turn to the last resort of imposing negative interest rates. Former Treasury Secretary Larry Summers considers a 500 basis-point margin to be absolutely necessary to effectively combat a recession[6]. Kenneth Rogoff makes this point unequivocally: "*One day we will get a new severe financial crisis, and then we could need negative interest rates of minus six or minus five percent to get out of the crisis quickly.*[7]"

1. See "Fed's Yellen expects no new financial crisis in 'our lifetimes'", Reuters, 27 June 2017. **2.** See "Yellen sieht Gefahr neuer Finanzkrise" ("Yellen sees risk of new financial crisis"), Frankfurter Allgemeine Zeitung, 12 December 2018. **3.** For example, the EU Commission has recently cut its growth forecast for the Eurozone for 2019 from 1.9% to 1.3%, see European Commission: European Economic Forecast. Winter 2019. 7 February 2019. Global economic growth, too, continues to weaken. The World Bank expects only 2.9% now (previously 3.0%), see "Darkening Prospects: Global Economy to Slow to 2.9 percent in 2019 as Trade, Investment Weaken", The World Bank, 8 January 2019; "European Economic Forecast – Winter 2019", EU Commission, February 2019 **4.** www.federalreserve.gov/econres/notes/feds-notes/predicting-recession-probabilities-using-the-slope-of-the-yield-curve-20180301.htm. **5.** The Fed cut its interest rates by an average of 5.5 percentage points in the nine recessions since the mid-1950s, a level that is impossible now given the current low rates – unless negative rates are on the table. **6.** See "Summers Warns the Biggest Economies Are Not Prepared for Another Recession", Bloomberg, 18 June 2018. **7.** "Star-Ökonom für Minuszinsen von bis zu sechs Prozent" ("Star economist for negative interest rates of up to six percent"), welt de, 18 September 2016 (our translation).

GOLD PERFORMANCE DURING US RECESSIONS

Decade	Gold Start (USD/oz)	Gold End (USD/oz)	Change (%)
11/1973 - 03/1975	100	178	78.0%
01/1980 - 07/1980	512	614	20.0%
07/1981 - 11/1982	422	436	3.3%
07/1990 - 03/1991	352	356	1.0%
03/2001 - 11/2001	266	275	3.5%
12/2007 - 06/2009	783	930	18.8%
Mean			20.8%

Source: Incrementum AG

NOW WHAT DOES THAT MEAN FOR GOLD INVESTORS?

In our previous, *In Gold We Trust* report, we already answered the question: "How does the gold price perform in recessions?" The short answer was: "Very well!"

GOLD PERFORMANCE DURING US RECESSIONS

The reasoning behind this performance seems logical. On the one hand, investors are looking for safe havens in times of crisis, and gold is the classical safe-haven asset. On the other hand, many investors will anticipate monetary and fiscal stimuli, and buy gold for inflation protection.

We wanted to analyse the development of gold and stock prices throughout recessions with more granularity.

Therefore, we have subdivided all recessions since 1970 into four phases:

- **Phase 1:** the run-up (one quarter before the recession hits)
- **Phase 2:** unofficial recession (the period from the outbreak of the recession to the official release of the GDP growth figures by the statistics office – assumption: one quarter)
- **Phase 3:** official recession
- **Phase 4:** last quarter of the recession

Although this may come as a surprise, there is no internationally standardised definition of the term 'recession'. Whereas the decline of real GDP for two subsequent quarters is considered a technical recession in the euro area, recessions are determined differently in the US. According to the National Bureau of Economic Research (NBER), an economy is in recession if a significant decline in economic activity seizes the majority of the economy and lasts for several months. Indicators are, among others, trends in GDP, real income, employment and industrial production. It is worth mentioning that tumbling stock markets are not taken into account in assessing whether the economy is in a recession or not.

12 MONTHS PASSED FROM THE ACTUAL START OF THE RECESSION TO ITS OFFICIAL DIAGNOSIS BY THE NATIONAL BUREAU OF ECONOMIC RESEARCH

For investors, the problem with both definitions is that a recession is usually only diagnosed once the economy is already past the worst.

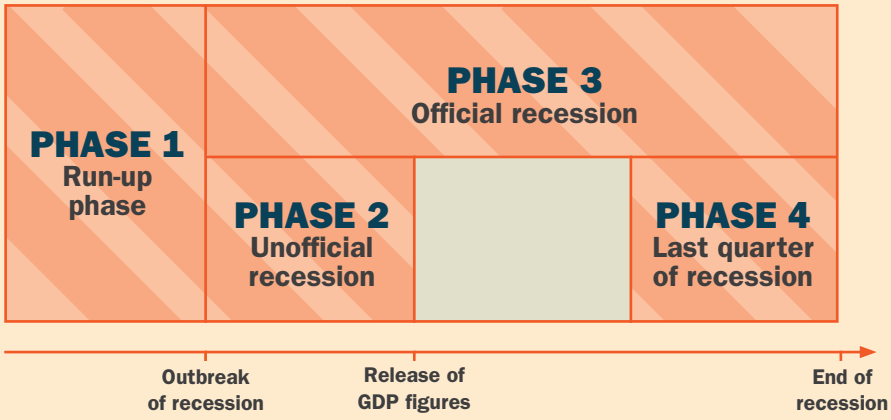
The deep recession in the aftermath of the Great Financial Crisis of 2007/2008 is a case in point. An unbelievable 12 months passed from the actual start of the recession to its official diagnosis by the National Bureau of Economic Research.

THE MAIN CHARACTERISTICS OF THE FOUR PHASES

Phase 1: the run-up

The run-up phase is defined as the short period of time that marks the transition from the economic boom phase to recession. It is also characterised by the transition from falling, but still positive, growth rates to negative growth rates. Another feature of the run-up phase is the continued increase in consumer prices. This should not surprise anyone who is familiar with the Austrian Business Cycle Theory. In the preceding boom phase, loose monetary policy will have incited additional investments whose completion now requires additional, but often not directly accessible, resources.

SEQUENCE OF PHASES



Source: Incrementum AG

This leads to higher rates of price increases, which were not anticipated during the investment decision-making process. The leaps in prices point up the economic inefficiency of some investment projects. These need to be suspended or written off, heralding the recession.

TO THIS EXTENT, GOLD AND THE US DOLLAR SEEM TO HAVE LIVED UP TO THEIR REPUTATION AS SAFE HAVENS

Phase 2: unofficial recession

The unofficial recession phase stretches from the actual beginning of the recession to the official announcement of the recession. This period of time, which typically lasts about one quarter, is particularly interesting because, at this point, the recessionary shrinking of the economy has not been officially confirmed. The emerging recession is supported only by leading indicators such as surveys, but not by hard facts. At this point, it is still unclear whether the economy will only be taking a breather or an actual recession is imminent.

Phase 3: official recession

The third phase is the official recession. It covers the entire duration of the recession, i.e. from the beginning of phase 2 to the end of phase 4.

An analysis of the data immediately reveals that both gold and the US dollar index have posted gains on average during the official recession phases: gold was up 20.2% (see table below) and the US dollar appreciated by 4.2%. To this extent, gold and the US dollar seem to have lived up to their reputation as safe havens. We can also see that the monetary policy of the central bank during this phase was clearly expansionary. The effective Fed funds rate decreased across all the recessions we analysed.

Phase 4: the final quarter of the recession

Phase 4 spans the final quarter of the recession. It is a fair assumption to make that, at this point, the stock market has already anticipated that the recession is ending. Also, by this late stage of the recession, drastic measures in monetary and fiscal policy will have been taken in reaction to the crisis.

Low interest rates and fiscal stimulus measures create a sense of optimism in the market even if they often fail to remedy the underlying cause of the crisis.

OVERVIEW: PERFORMANCE OF THE S&P 500 AND GOLD, IN USD AND EUR, IN %, 1970-2018

		S&P 500				Gold in USD				Gold in EUR			
	Recession duration	Phase 1	Phase 2	Phase 3	Phase 4	Phase 1	Phase 2	Phase 3	Phase 4	Phase 1	Phase 2	Phase 3	Phase 4
1st Recession	Q1/1970 - Q4/1970	-1.8%	-4.6%	-7.0%	7.0%	-8.9%	-6.6%	0.0%	5.9%	N/A	4.6%	11.1%	3.0%
2nd Recession	Q1/1974 - Q1/1975	-8.0%	0.3%	-15.0%	16.6%	-10.9%	58.5%	89.7%	-1.1%	7.2%	51.8%	51.0%	-6.2%
3rd Recession	Q2/1980 - Q3/1980	7.1%	-2.1%	7.7%	10.0%	70.1%	-22.8%	-5.9%	21.8%	27.5%	0.5%	20.2%	-1.6%
4th Recession	Q4/1981 - Q4/1982	-7.4%	2.9%	12.8%	15.9%	-14.6%	0.8%	1.2%	14.2%	2.6%	-4.8%	21.0%	10.4%
5th Recession	Q4/1990 - Q1/1991	-10.7%	-0.1%	13.8%	13.9%	7.1%	-3.3%	-7.9%	-4.7%	4.6%	-9.3%	-12.2%	-3.6%
6th Recession	Q2/2001 - Q4/2001	-5.7%	1.3%	-8.1%	0.5%	-1.5%	3.8%	5.4%	1.3%	-0.8%	8.3%	5.5%	-4.4%
7th Recession	Q1/2008 - Q2/2009	0.5%	-10.2%	-50.4%	-18.0%	21.6%	14.3%	16.3%	24.0%	2.2%	12.2%	31.4%	19.8%
	Average:	**-3.9%**	**-1.9%**	**-10.5%**	**5.9%**	**6.1%**	**4.1%**	**20.2%**	**8.3%**	**6.8%**	**7.6%**	**22.8%**	**2.1%**

Therefore, one would expect stocks to pick up momentum and perform positively in the final phase.

GOLD POSTED SIGNIFICANT AVERAGE GAINS ACROSS THE ENTIRE RECESSIONARY CYCLE BOTH IN US DOLLARS AND IN EUROS IN EVERY PHASE

The table on page 25 contains the performance of gold and the S&P 500 during the four different phases of seven different recessions. We have also added the performance of gold in euros.

Remarkably, gold posted significant average gains across the entire recessionary cycle both in US dollars and in euros in every phase, whereas stocks (as measured by the S&P 500) recorded profits only in the final stage of the recessions. Thus, gold managed very well to compensate for the stock losses in phases 1, 2 and 3. Also, the higher the losses of the S&P 500, the better gold performed.

In summary, gold has been excellent at offsetting stock losses during recessions. Thus, we would expect gold to record substantial gains and act as a hedge against bear stock markets in the future as well. However, we are less optimistic about bonds, the classic stock diversifier. High debt, the zombification of the economy and monetary policy that is still very loose by historical standards combine to undermine the ability of bonds to act as a stock diversifier. Therefore, gold is positioned to remain an indispensable component of the portfolio in the future, as it lets the investor navigate stressful passages in the market with relative ease.

CONCLUSION

- Recession risks are significantly higher than discounted by the market. The last two recessions, in 2000 and 2008, prompted the Federal Reserve to cut interest rates by 550 and 525 basis points respectively, and in the nine recessions since the mid-1950s, by an average of 550 basis points.
- The lower the key interest rate set by the central bank, the lower the opportunity costs of holding gold compared to investing in bonds or holding money in a bank account. Lower interest rates should thus support the gold price.
- In the event of a downturn, negative interest rates, a new round of QE and the implementation of even more extreme monetary policy ideas (e.g. MMT) are to be expected.
- As holding gold does not imply facing a counterparty risk, gold is a safeguard against a credit default crisis, which does not only annihilate liabilities but also financial assets and to the same extent.
- In case of a significant surge in (consumer price) inflation, gold protects against the concomitant loss in purchasing power. This was the case in the 1970s and early 1980s in the US, and more recently in Venezuela and Turkey. But even in times of acceptable inflation, i.e. around 2% per year, gold fulfils its task as a protection shield against the loss in purchasing power over the medium term.
- Given this scenario, we think that gold harbours better opportunities than bonds with respect to its future suitability as a stock diversifier. The following simple relationship holds true for bear stock markets – the looser the monetary policy, the better for gold.

WE WOULD EXPECT GOLD TO RECORD SUBSTANTIAL GAINS AND ACT AS A HEDGE AGAINST BEAR STOCK MARKETS IN THE FUTURE AS WELL.

Ronnie is a managing partner at Incrementum AG and is responsible for Research and Portfolio Management. In 2007, he published his first *In Gold We Trust* report. Over the years, the *In Gold We Trust* report has proceeded to become one of the benchmark publications on gold, money and inflation.

Since 2013, Ronnie has held the position as reader at Scholarium in Vienna, and he also speaks at Wiener Börse Akademie (i.e. the Vienna Stock Exchange Academy). In 2014, he co-authored the international bestseller *Austrian School for Investors* and, in 2019, *Die Nullzinsfalle (The Zero Interest Rate Trap)*. Moreover, he is an advisor for Tudor Gold Corp. (TUD), a significant explorer in British Columbia's Golden Triangle.

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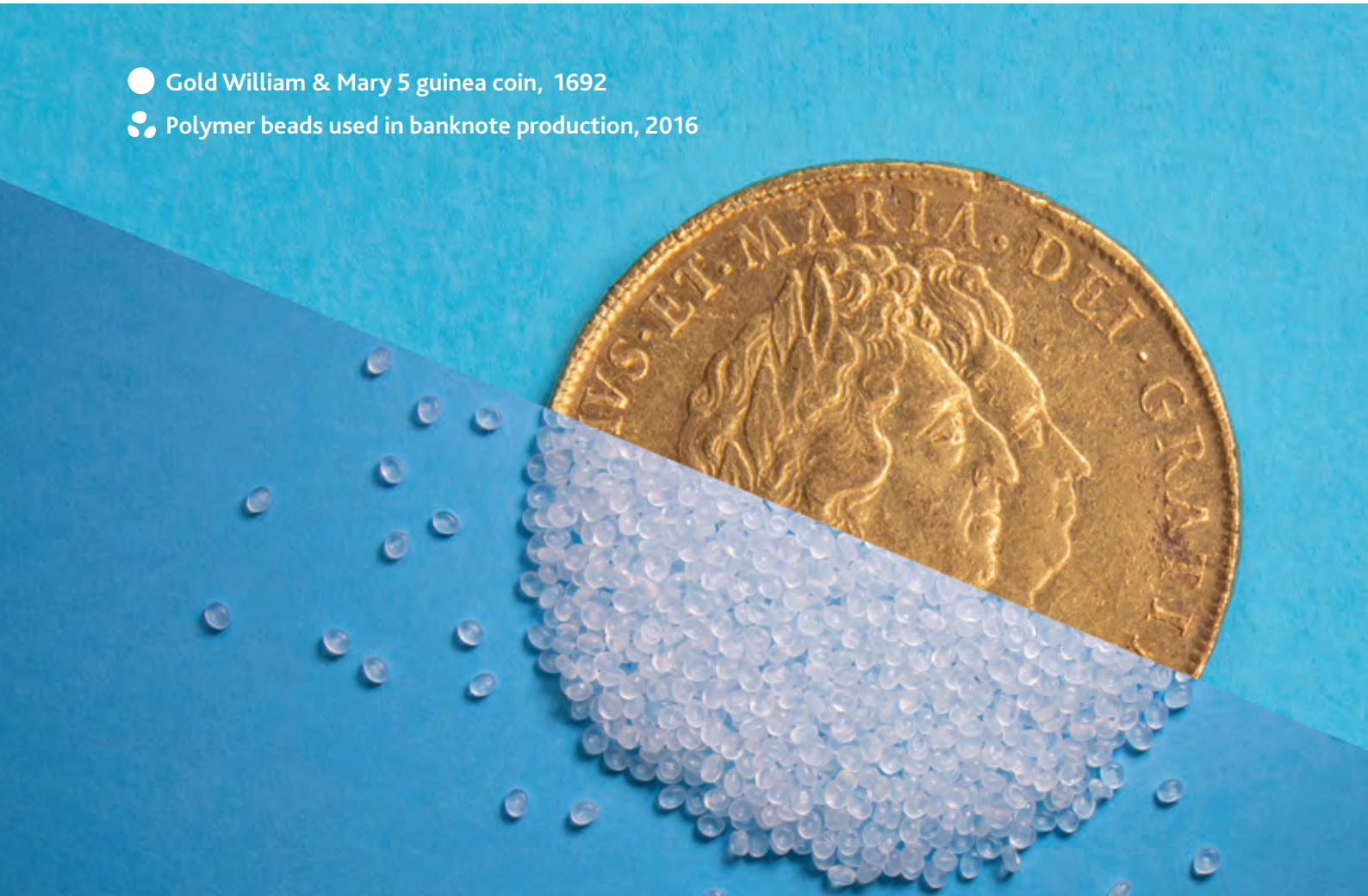

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FACING FACTS

HEDGING REMAINS STAGNANT

BY FEDERICO GAY, PRECIOUS METALS SUPPLY ANALYST, GFMS, REFINITIV

Lower global economic growth expectations, increasing tensions between the US and Iran, rumours surrounding further rate cuts by the US Federal Reserve and the ongoing trade war amongst the two largest economies are fuelling an optimistic scenario for gold prices. In this environment, gold miners are resilient to expand their hedge book in order to avoid capping the upside earning potential.

ADDING UP TO

58.6

TONNES

POLYUS HOLDS THE LARGEST NOMINAL HEDGE BOOK, WHICH ADDS UP TO 1.89 MOZ, REPRESENTING 19% OF THE GLOBAL TOTAL

The delta-adjusted hedge book contracted by 0.8 Moz (25 tonnes) during Q1 2019, representing a 12% decrease compared to Q4 2018. As a result, the hedge book stood at a total of 6.24 Moz (194 tonnes) at the end of March. Our records show that during the last quarter, 30 companies took a net de-hedging position, while only 10 were net hedgers. Amongst the last group, the largest hedger was Gold Fields, after increasing its options and forwards contracts by 0.12 Moz (3.6 tonnes), mainly at its Australian-based operations. The company holds the second-largest nominal hedge book, totalling 1.06 Moz (32.9 tonnes). Other net hedgers include Harmony Gold and Resolute Mining, with a combined 0.08 Moz (2.6 tonnes). Hedging activity remains strong mainly in Australia, where the Aussie dollar has depreciated around 12% since January 2018, pushing companies to secure favourable gold prices in the local currency.

According to our estimations, over 45% of the total hedge book is represented by Australian-based miners, whose hedging has increased considerably over the last few years.

Turning to the net de-hedgers, Russian-based Polyus Gold has remained at the top for two consecutive years, as it continues to exercise its barrier options, which are part of the Strategic Price Protection Programme signed in Q1 2014. Polyus holds the largest nominal hedge book, which adds up to 1.89 Moz (58.6 tonnes), representing 19% of the global total. Further de-hedging activity was posted during the last quarter by Fresnillo plc, as over 0.17 Moz (5 tonnes) of options matured during this period, while Newcrest delivered 0.12 Moz (3.6 tonnes). The Australian company hedged a portion of Telfer's production until 2023, locking in near record-high gold prices back in 2016.

AFTER PEAKING DURING THE BREXIT REFERENDUM IN Q2 2016, HEDGING HAS CONTRACTED BY 2.6 MOZ (83 TONNES) DURING THE LAST THREE YEARS

The delivery schedule for the rest of the year is 2.38 Moz (74 tonnes), of which around 0.87 Moz (27 tonnes) are due to mature during Q2 2019. Even though some gold producers have already decided to increase their hedge books, the bulk of contracts during the recent months are relatively modest compared to historical data.

For example, Saracen Holdings added 0.05 Moz (1 tonne) of hedging at AUD$1,888/oz, though it delivered 0.07 Moz (2 tonnes) during Q1 2019. Resolute Mining, which has been an active hedging player during the past year, hedged an additional 0.06 Moz (2 tonnes), divided in equal parts both in Australian and US dollars.

In addition to the previously mentioned bullish sentiment over gold prices, mining companies are leaning towards other capitalisation instruments such as gold streaming, which also helps them avoid generating further debt.

TOP 10 NOMINAL HEDGE BOOK HOLDERS

		Moz	Tonnes	% Total
1	Polyus Gold	1.89	58.6	19%
2	Gold Fields Ltd	1.06	32.9	11%
3	Newcrest	0.88	27.4	9%
4	Penoles	0.69	21.4	7%
5	Harmony Gold	0.58	18.2	6%
6	Fresnillo Plc	0.52	16.1	5%
7	Regis Resources	0.44	13.6	4%
8	Evolution Mining	0.44	13.6	4%
9	Saracen Mineral Holdings	0.36	11.2	4%
10	Northern Star Resources	0.34	10.6	3%
	Others	2.84	88	28%
	TOTAL	**10.03**	**312**	

Source: GFMS, Refinitiv

Federico Gay, Senior Analyst, Refinitiv, GFMS. Federico is a geologist with a BSc from the National University of the South, Argentina. He joined Refinitiv in London in November 2019, focused on precious metals supply modelling. Prior to Refinitiv, he worked over seven years in Chile in a wide range of assignments, including exploration, ore control, geological modelling and resource estimation for a Copper-Gold-Molybdenum mine in the Atacama Desert. He completed a master's program in Economic Geology from the Catholic University of the North, Chile.

45%

ACCORDING TO OUR ESTIMATIONS, OVER 45% OF THE TOTAL HEDGE BOOK IS REPRESENTED BY AUSTRALIAN-BASED MINERS, WHOSE HEDGING HAS INCREASED CONSIDERABLY OVER THE LAST FEW YEARS

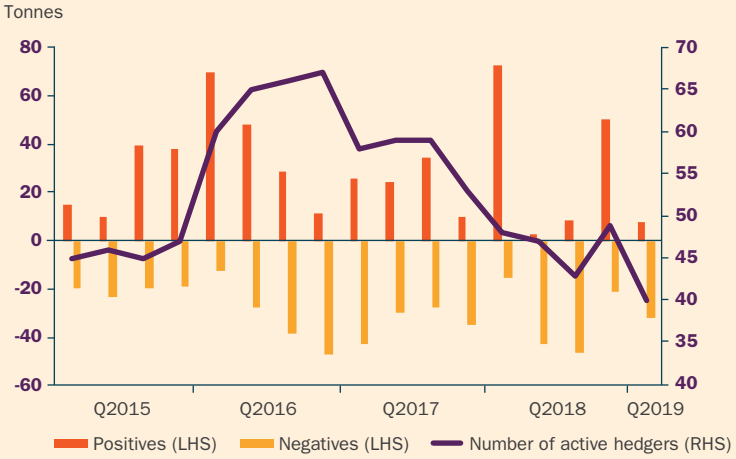
The sum of these factors is, in my opinion, taking producers' focus off hedging. If we analyse the 10-year history regarding the global hedge book, on a delta basis, hedging virtually disappeared during the global economic growth period that followed the 2008 crisis, followed by a sluggish recovery at the start of 2014. After peaking during the Brexit referendum in Q2 2016, hedging has contracted by 2.6 Moz (83 tonnes) during the last three years.

After hitting a six-year high of US$1,438/oz, gold prices fell sharply following the resumption of trade talks and positive rhetoric between China and the US at the G20 summit, which took place in Osaka, stabilising afterwards at around US$1,400/oz.

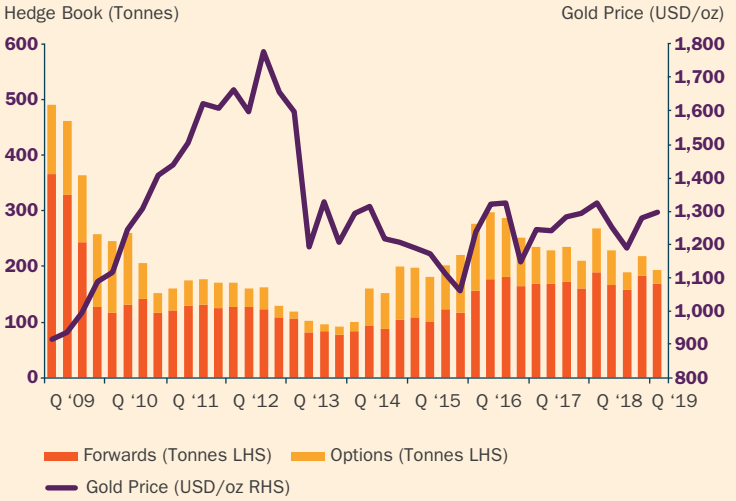
WE ESTIMATE THAT HEDGING WILL CONTINUE TO CONTRACT DURING THE NEXT MONTHS, ONLY RECOVERING IN Q4

While the scenario may change after the Federal Reserve unveils its strategy in the next few days, we at GFMS estimate that hedging will continue to contract during the next months, only recovering in Q4 as several Australian and Russian companies will reach a low hedge ratio (which accounts for covered production compared to the expected deliverable ounces for the period), possibly triggering new hedges.

ACTIVE HEDGE BOOK HOLDERS



GLOBAL DELTA-HEDGE BOOK: 10-YEAR HISTORY



MARKET MOVES

BOB DAVIS AND BRIAN GROARK JOIN SCOTIABANK

Bob Davis has joined Scotiabank in London as Director, Head of Sales and Origination, Commodity Derivatives for EMEA. He has over 30 years' experience in the metals markets, and was previously the regional head of Metals Trading and Sales at Toronto-Dominion Bank. He has also held key roles at BNP Paribas and JP Morgan Chase.

Brian Groark has joined Scotiabank in New York as Associate Director, Commodity Sales. He has nearly ten years' experience in the metals markets and was previously at HSBC Bank and Mitsui Precious Metals.

REGULATION UPDATE

BY RACHEL HART, LAWYER, LBMA

Rachel Hart, Lawyer, LBMA. Deals with legal and compliance matters affecting the precious metals market, including financial regulation and the Responsible Sourcing Programme. She has taken responsibility on a number of initiatives and helps to manage any relevant legal work on behalf of LPMCL, as well as support the market on the application of REACH and the Global Precious Metals Code.

Before joining the LBMA, Rachel worked as a Finance Knowledge Assistant at Freshfields Bruckhaus Deringer, specialising in structured finance and debt capital markets. She read law at University of York and University of Law, London.

Net Stable Funding Ratio

LBMA is reaching out to central banks for their support on NSFR lobbying.

By way of reminder, the Capital Requirements Regulation (CRR) II framework will require 85% of Required Stable Funding (RSF) to be applied to certain precious metals transactions from 2021.

LBMA and LPMCL have been working with Norton Rose Fulbright LLP to advocate a lower RSF factor. In July 2018, the European Parliament's Committee on Economic and Monetary Affairs (ECON) adopted an amendment lowering the RSF to 50%. However, when put to the European Commission and member states in November 2018, this proposal was rejected. Instead, the 85% RSF will go ahead for the financing and the clearing and settlement of precious metals transactions.

LBMA IS REACHING OUT TO CENTRAL BANKS FOR THEIR SUPPORT ON NSFR LOBBYING

The European Banking Authority (EBA) will be the authority responsible for any future reductions to the RSF, and it has two years to finalise its findings. Under the LBMA-i trade reporting initiative, LBMA has analysed the reported data to demonstrate the levels of liquidity and transparency within the precious metals market to assist with the EBA's assessment. The objective of any upcoming advocacy activities remains to secure a full exemption from the application of the RSF for precious metals clearing and settlement services and for financing transactions.

House of Commons Debate: Precious Metals Markets

On 8 July, the House of Commons held a debate on the risk of manipulation of the precious metals markets. The debate was led by Jeremy Lefroy, a Conservative MP for Stafford. Mr Lefroy raised the debate to discuss whether UK's regulatory approach to precious metals was robust enough to deal with market manipulation. Mr Lefroy referred to the spoofing cases in recent years in the US and questioned whether similar activity could occur in the UK. In conclusion, Mr Lefroy suggested that the Government commission an enquiry into the bullion market, particularly in the UK.

ON 8 JULY, THE HOUSE OF COMMONS HELD A DEBATE ON THE RISK OF MANIPULATION OF THE PRECIOUS METALS MARKETS

John Glen, a Conservative MP, and Economic Secretary to the Treasury and City Minister, led the response.

The precious metals' markets applicability to the Market Abuse Regulation, the UK and EU benchmarks regimes, and LBMA's Global Precious Metals Code were referenced throughout the response. Mr Glen concluded that under this robust regulatory framework, the FCA had the necessary tools to detect and respond to attempts at market manipulation.

Mr Glen advised that HM Treasury would not consider it necessary to undertake any reform of the UK's regulatory regime in its application to precious metals markets or to commission a Government inquiry or review.

A transcript of the debate is available on Hansard.

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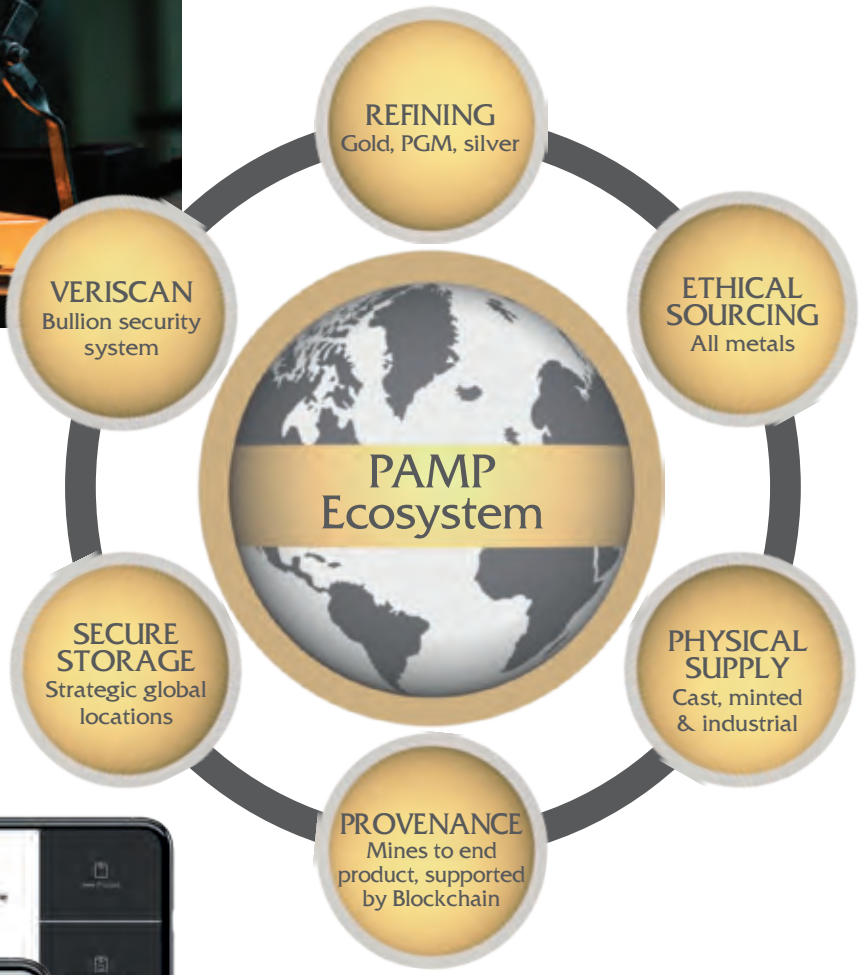

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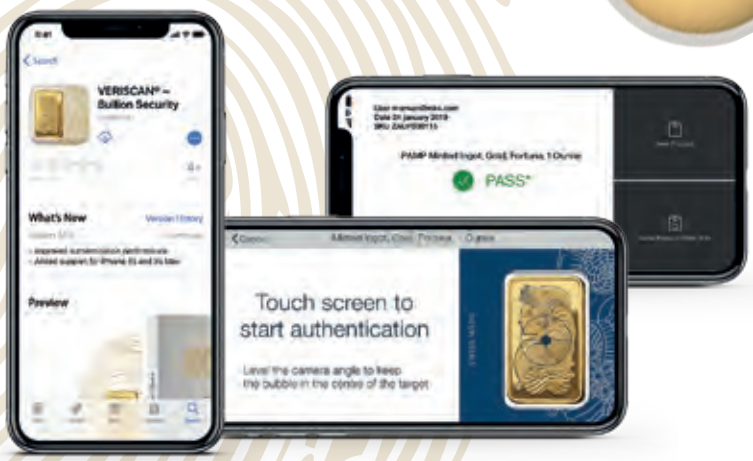

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