FACING FACTS

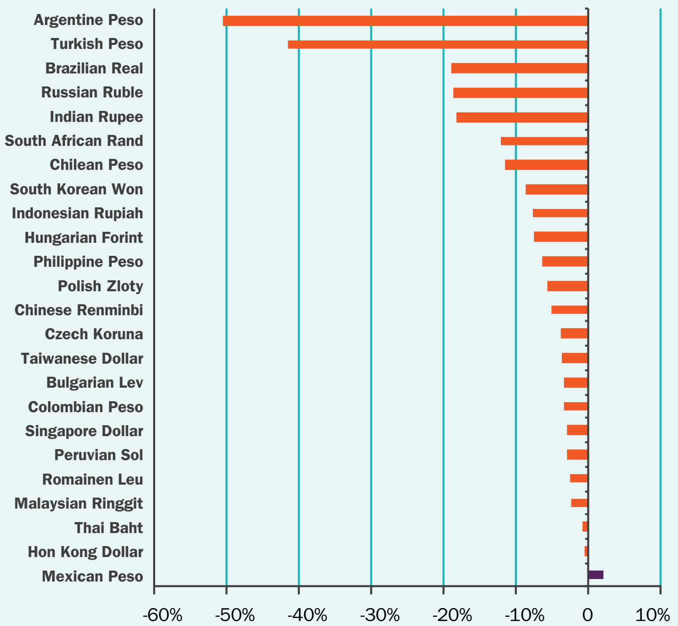
CENTRAL BANK GOLD HOLDINGS RISE AS EMERGING MARKETS DIVERSIFY THEIR RESERVES

BY NATALIE SCOTT-GRAY, METALS DEMAND ANALYST – RESEARCH AND FORECASTS, GFMS, REFINITIV

Central bank gold holdings jumped in the second quarter (Q2), rising by 35% or 106 tonnes year-on-year to their highest level since (Q3) 2017. With struggling emerging market economies plunged further into turmoil on the back of a global trade war, rising yields and a strengthening US dollar, central banks pursued safe-haven protection in the form of gold while reducing their exposure to foreign exchange reserves.

EMERGING MARKETS DIVERSITY AWAY FROM THE US DOLLAR

EMERGING MARKETS CURRENCIES YEAR-TO-DATE

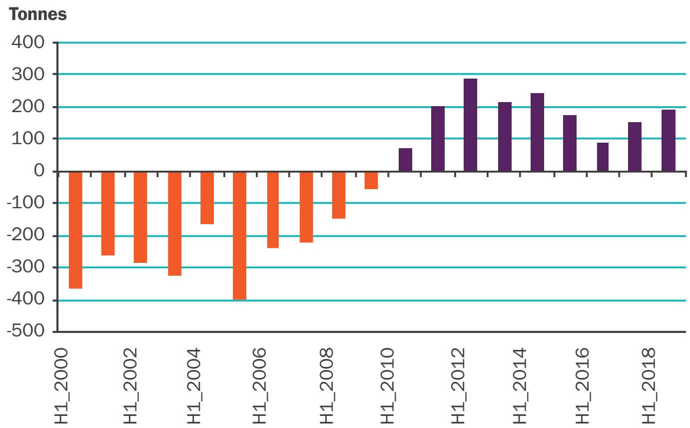


In the first six months of the year (H1), central banks increased their gold holdings by 27% or 191 tonnes in comparison to the same period a year ago. This marks the ninth consecutive year of H1 purchases of gold, having previously recorded sales in H1 over the 2000-2009 period (and may well have had, initially, something to do with the financial crisis).

RUSSIA BUYS FOREIGN EXCHANGE RESERVES AS OIL PRICES RISE – GOLD INCLUDED

For the sixth consecutive year, the Russian Central Bank maintained its position as the largest acquirer of gold in H1, purchasing 105 tonnes and bringing total gold holdings to 1,944 tonnes, firmly placing it as the fifth-largest gold holding country in the world (behind the United States, Germany, Italy and France and above China). Despite rising oil prices (which have averaged $72/bbl this year) and Russia's Finance Minister endorsing the increased purchase of foreign exchange reserves (including US dollars) when oil prices average over $40/bbl, the central bank's purchases of gold rose to their highest level in H1 in this century. The implementation and threat of further US and EU sanctions this year in response to the crisis in Ukraine and chemical (and biological) warfare that took place in the UK in April, has resulted in the rouble weakening, falling by 21% intra-year. Indeed, The World Bank has lowered its forecast for the country's economic growth from 1.7% to 1.5% for 2018.

OFFICIAL SECTOR GOLD PURCHASES AND SALES (H1 PERIOD)



TURKEY

The Central Bank of Turkey (CBRT) was the second-largest purchaser of gold in H1, with gold holdings increasing by 38 tonnes. The local currency had fallen by 40% (at the time of writing), on the back of concerns over foreign currency debts (largely built on US dollars), in addition to the country's strained relationships with both the United States and Germany. The CBRT continued to seek economic independence, diversifying away from its foreign exchange reserves in favour of gold.

INDIA

In a similar stead, India, which is the 11th largest gold holder globally, purchased gold for first time this century at 8 tonnes. Fears over global risks, market volatility and rising yields in the West have encouraged markets to limit their exposure to the US dollar.

ARGENTINA

In Argentina, following the sale of foreign currency in the spot market to stabilise the peso, which had fallen to its lowest level on record, the country requested a bailout from the International Monetary Fund this year. Central bank purchases for the country rose by 7 tonnes, its largest H1 purchase since 2000.

VENEZUELA

While Venezuela has long been in economic turmoil, the country is now at breaking point, with a humanitarian crisis at hand and a currency which is almost valueless. A host of fresh US sanctions has limited the manoeuvrability of the country to raise money through international banks and targeted individuals close to the President. In order to boost liquidity for dwindling international reserves in the country, gold 'swap' deals took place over the last few years, drawing down gold reserves, with gold as a percentage of total reserves falling to their lowest level of 64.6% since July 2016. Over H1, Venezuela has tried to buy back its safe-haven asset, purchasing 2 tonnes. Elsewhere, purchases were made by Columbia and Mongolia, each acquiring 2 tonnes of gold.

SALES EXPECTED TO REMAIN LIMITED

While the scales were heavily tipped in favour of central banks purchasing gold in H1, sales were recorded over this period for countries such as Germany and Australia, at 4 tonnes each. It is likely that these transactions are part of each country's regular pattern of small-scale sales as part of their retrospective official coin programmes. Further sales (above 1 tonne) were recorded by Qatar, Sri Lanka and Ukraine.

MORE PURCHASES TO COME?

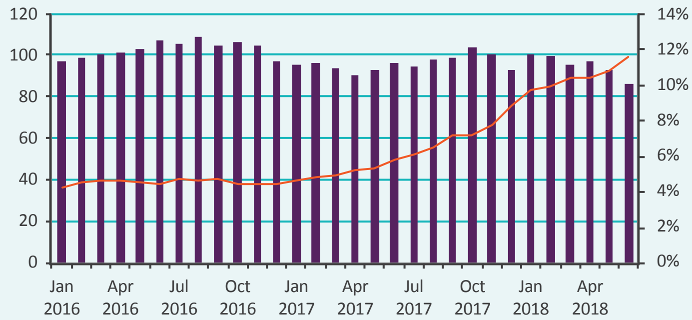
We forecast that central bank transactions, or net official purchases, will exceed levels set in 2017 at 450 tonnes. Gross sales levels, which have remained far below 2010 levels over the last seven years, are expected to remain weak. Gross purchases are likely to remain dominated by Russia, particularly in light of the threat of fresh sanctions from the West, while other emerging markets suffering from trade disputes and rising yields such as Turkey will continue to diversify away from the US dollar, where possible. China, which continues to hold a very low level (2.4%) of gold in its foreign exchange reserves (compared to most European countries, which hold between 60% and 80%), is similarly expected to build holdings (despite not reporting a change since October 2016).

REPATRIATION

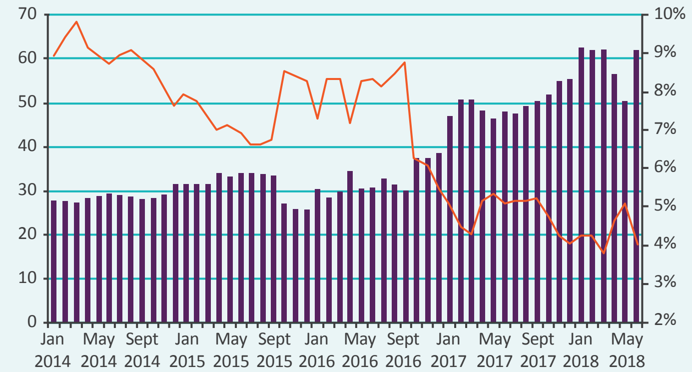
Repatriation of gold reserves by central banks has become a common theme over the last few years, with Germany, the second-largest gold holder in the world (with total reserves standing at 3,370 tonnes at end-June), announcing in August last year that it had completed its four-year repatriation operation (which was first announced in 2013). A total of 674 tonnes of gold were moved from the Banque de France and the Federal Reserve Bank of New York, back to its own vaults. The move was originally set to be completed by 2020. Adding to this theme, the Hungarian National Bank (MNB) announced in March this year that it intends to take back all its gold reserves (3 tonnes or 98,000 ounces) currently stored in the Bank of England.

Natalie Scott-Gray is a Metals Demand Analyst at GFMS, Refinitiv. She is the key analyst covering materials used in rechargeable batteries, predominately utilised in both the automotive and power grid sectors. She is the lead analyst for the GFMS coverage on cross commodities, in addition to heading up the team's technical analysis across the metals space. Furthermore, she is responsible for covering metal demand in the European markets. Prior to GFMS, Natalie was an oil and gas upstream analyst. She holds a Masters Degree in Chemistry from the University of Edinburgh.

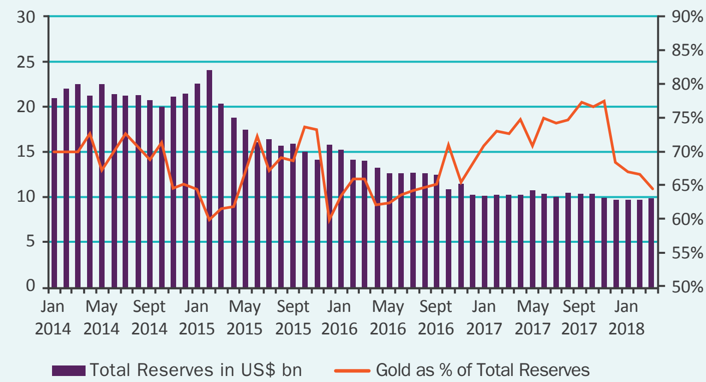
TURKISH TOTAL RESERVES AND GOLD AS A PERCENTAGE OF TOTAL RESERVES (CALCULATED USING THE MONTHLY AVERAGE JUNE 2018 GOLD PRICE)



ARGENTINIAN TOTAL RESERVES AND GOLD AS A PERCENTAGE OF TOTAL RESERVES (CALCULATED USING THE MONTHLY AVERAGE JUNE 2018 GOLD PRICE)



VENEZUELAN TOTAL RESERVES AND GOLD AS A PERCENTAGE OF TOTAL RESERVES (CALCULATED USING THE MONTHLY AVERAGE JUNE 2018 GOLD PRICE)



The *Alchemist* is published quarterly by LBMA. If you would like to contribute an article to the Alchemist or if you require further information please contact the Editor, Aelred Connelly, LBMA, 1-2 Royal Exchange Buildings, Royal Exchange, London EC3V 3LF
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