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Publication of *Gold Survey 2007*

Sustained Investment plus Lower Official Sector Sales and Ongoing De-Hedging Key to 2006's Price Gains & to Potential for Fresh Highs in 2007

GFMS launched *Gold Survey 2007* today, an edition that marks the 40th anniversary of their authoritative annual survey of the world gold market, at events in London, Toronto and Johannesburg. The following details some of the highlights of the *Gold Survey* from the briefing given at the London launch by Philip Klapwijk, chairman of the independent precious metals research consultancy.

The potential for gold to post fresh highs in 2007 and 2008 was a key theme brought out in the commentary surrounding the launch. Klapwijk noted, "it's looking pretty certain that the record in terms of the annual average, $614.50 back in 1980, is going to fall this year. I'd also be far from surprised if this year we saw the market moving above the 2006 high of $725. Quite whether we'd then get close to the all time high of $850 is more doubtful, but I'd certainly expect the upward price trend to continue on into 2008".

GFMS see this upside potential as being firmly in the hands of investors. This year's *Gold Survey* actually recorded a fall for 2006 in implied net investment, the consultancy's proxy for western investment, but as Klapwijk added, "investment may have dipped a little on 2005's levels but that's just a reflection of the swing from a mainly buy side market to one with both an active buy and sell side. And the vast bulk of the selling we saw last year was just profit taking or stop loss selling in the wake of the May spike. We're not really seeing any evidence of investors starting to shun the metal for the long term".

The *Survey* states how the rationale for investor confidence in the medium and long term prospects for gold during 2006 and moving forward was little changed on the previous year. The chief explanations of this that GFMS highlighted were actual and potential dollar weakness, a possibly sharp slowdown in the US economy and the damage this would inflict on conventional asset returns, the threat of higher inflation and an escalation of geopolitical tensions, most obviously as regards US action against Iran. The consultancy also cautioned against the risk of ignoring the 'weight of money' argument, pointing out that one measure of institutional investment to date, the value of the combined non-commercial position in 13 commodities, had at end-2006 reached 'only' $138 billion or far less than the market capitalisation of some blue-chip equities.

That investment could drive the price higher last year and has the potential to do so this year GFMS believe was partly due to the low level of net official sector sales. Klapwijk added, "we lost around 350 tonnes of supply from official selling last year and not only did that impact the market directly but also the implied shift in central bankers' stance on gold was good for investor confidence. And looking at 2007, we'd expect to see the CBGA [Central Bank Gold Agreement] countries undershooting quota and for the rest of the world to remain small net purchasers. All this can happen without any of the larger dollar holders, like China, emerging as substantial buyers - something we don't see happening imminently".

The consultancy also highlights the importance of producer de-hedging last year as this quadrupled to over 370 tonnes and GFMS expect this to be maintained at elevated levels this year. Klapwijk noted, "we're probably going to see a slightly lower level of support from de-hedging in 2007 but that's almost entirely due to exceptional corporate restructurings in early 2006. There's no sign as yet of producers losing their nerve over the price and starting to put in place significant strategic hedges".

One of the main areas of weakness last year was jewellery fabrication and its converse, old scrap, with the former contracting sharply and the latter growing strongly. However, growing acceptance of higher prices and lower volatility in the second half of 2006 actually enabled jewellery demand to rebound strongly on first half levels. GFMS therefore see this as providing a higher 'floor' for the price, with jewellery related buying being expected to step in as and when investment and the price look a little soft. The suddenness of the rally last year was also thought to have precipitated a marked shake out of tired trade stocks, something not thought likely to be repeated this year. In fact, GFMS foresee a rise in scrap as unlikely until prices are well over the $700 mark.

A brief mention should perhaps be made of the main element of supply, mine production. The *Survey* noted a fall in 2006 to a 10-year low but this did little to ignite the price as this only mid-sized change was well telegraphed and the market was generally aware of the likelihood of a recovery in 2007 back to levels not dissimilar to 2005.

The statistical highlights of the report are outlined overleaf:

Supply Highlights

- Global **mine production** last year fell by 3% to a ten-year low. On a regional basis, losses were greatest in Asia, despite gains in China, whilst notable falls were also recorded in North America, Africa and Oceania. Latin America was the sole area to see any growth of note, though new mines in Africa meant that, if we exclude South Africa, the continent actually saw a modest gain.

- Global **cash costs** in US dollar terms rose by $45/oz in 2006, due mainly to inflated energy, consumables and labour charges.

- Net **official sector sales** more than halved in 2006 to their lowest level since 1997. This was the result of both a fall in CBGA sales (which in the 2005/06 Agreement year were more than 100 tonnes under quota) and a swing by other countries to small scale net purchases. Central bank lending fell yet further in 2006, by not far off 400 tonnes, due mainly again to low leasing rates.

- **Scrap** surged by around a quarter to record levels just over 1,100 tonnes. The traditionally price sensitive countries saw the bulk of the gains (though India was unusual in that its scrap slipped) but volumes in the industrialised world also grew strongly.

Demand Highlights

- **Jewellery fabrication** in 2006 fell by 16% (though its call on the bullion market, as expressed in offtake excluding scrap, dropped by over 20%). The first and second halves of the year, however, were markedly different, with the former suffering a near 30% slump (year-on-year) and the latter just managing a rise. Some of the greatest losses were seen in the Middle East and East Asia, though, largely thanks to robust GDP growth, China even saw slight growth while India's decline was comparatively muted. Heavy western trade destocking was key to the sharp fabrication losses in Italy and slump in US imports. **Other fabrication** grew by just over 10% last year, with strong gains seen in electronics, official coins and imitation coins and only small losses in dental.

- Last year saw a slip of almost 20% in **implied net investment** to a little under 400 tonnes. This decline was a reflection of the swing from a buy side dominated 2005 to a more two-way market, with activity on both the buy and sell sides. This change was largely a function of the stop loss selling and heavy profit taking emerging after the May high, as suggested by the disinvestment apparent on the main commodity exchanges. Other institutional and high net worth arenas such as the OTC market, in contrast, saw increased levels of interest. More retail focused areas of investment tended to remain quiet in 2006. Last year saw a 14% decline in (non-western) **bar hoarding** though this seemingly mid-sized change masks the major gains seen in India and Vietnam and the heavy losses in Japan.

- Producer **de-hedging** in 2006 more than quadrupled to just over 370 tonnes. This scale of the increase was somewhat unexpected as corporate activity impacted strongly on the first half (and whose volumes were almost three times those of the second half). At year-end, the combined producer hedge book stood at levels last recorded in 1994.

Note to Editors about GFMS Limited:
GFMS Limited is the world's foremost precious metals consultancy, specialising in research into the global gold, silver, platinum and palladium markets. GFMS is based in London, UK, but has representation in Australia, China, India, Spain, France, Germany and Russia, and a vast range of contacts and associates across the world.

Press Contacts: Philip Klapwijk or Paul Walker, GFMS Limited, Hedges House, 153-155 Regent Street, London, W1B 4JE, UK, tel: +44 (0)20 7478 1777, fax: +44 (0)20 7478 1779, email: gold@gfms.co.uk, web site: www.gfms.co.uk

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