PRESS RELEASE
London, 13th September 2007

Embargoed for publication or distribution by wire until 09:30 hrs London time on Thursday, 13th September 2007

Publication of *Gold Survey 2007 - Update 1*

Investor-Led Push over $700 Expected to Bring About $690 Second Half Price Average, with Further Gains in 2008 Expected

GFMS released *Gold Survey 2007 - Update 1* today, their latest report on the gold market. A summary of the findings of the report was given by Philip Klapwijk, Executive Chairman of GFMS, at a seminar in London organised by the precious metals consultancy.

A key feature of the *Update* is its forecast for all the supply and demand variables and the gold price itself. This the consultancy feels could reach a record level for a six-month average of $690 in the second half. Klapwijk noted, "GFMS' take on investment's potential to drive gold higher was the key to our forecast that the price would finally crack $700 this year. It's maybe breached that a bit earlier than we were expecting - as you'll notice in the printed report, which went to press a week or so back when we were still well below $700, we'd envisaged the rally being more a fourth quarter affair. But I don't think it'll be a problem sustaining these elevated levels. We may not be completely out the woods as regards speculator sell-offs to raise cash or reduce leverage in our new world of sub-prime jitters, but the norm of safe-haven buying should dominate investor activity from now on".

This buy-side interest was expected to be chiefly driven by 'traditional' factors, such as an anticipated fall in the value of the US dollar, lower economic growth and therefore equity values (particularly in the United States) and the possibility of cuts in interest rates, again mainly in the US in an attempt to forestall recession. A rally was thought possible without the aid of political developments, though it was added that prices should strengthen further "particularly if Middle East tensions escalate sharply".

The *Update* noted that heavy liquidations by short term speculative players, particularly in the second quarter this year, were the chief factor behind the first half recording sizeable implied net *dis*investment of over 200 tonnes. The consultancy feels this was very much the product of temporary overspills from non-gold issues, such as June's bond market crisis and the nature of disposals was strongly biased to profit taking or stop loss selling. GFMS report that there was scant evidence of any longer term investors losing confidence and instituting strategic shorts, a factor which they feel is crucial to the solidity of values moving forward.

Despite this, GFMS spelt out that the rally could only really be driven by investment, and that, having only one main support, price volatility could jump. A key reason for this stance is the slump in producer de-hedging, which the consultancy feels could drop from over 300 tonnes in the first half to under 80 in the second. Klapwijk added, "we're not seeing any real interest yet in strategic hedging. It's just that, with the hedge book a whole lot smaller than it was, you can't expect too much more of the heavy buy-backs we've seen in recent years". Mine production, however, was forecast to dip a fraction in the second half.

Another factor that GFMS believe will restrain the rally is the level of central bank selling, which is forecast to more than double in the second half. Klapwijk noted, "we'll probably see CBGA selling nudge towards the 500 tonne mark in this Agreement year and we'd expect sales moving forward to run at a fairly sustained level, and that's higher than we, and many others, were thinking would happen a few months back. But I think much of this increase got factored into the price a while ago, maybe when we had news from the likes of the Swiss on higher sales".

Fabrication demand was also forecast to rise in the second half but this was not expected to actively support any rally due to its price sensitive nature though it should provide good bedrock support to prices. The buoyant response of jewellery offtake in the first half, after all, was cited as a key reason as to why those investor sell-offs that did occur were normally well contained, with forays sub-$650 typically brief. While much was chiefly just a response to more stable gold prices, strong GDP growth in Asia was also seen as important and, with this region still expected to keep growing nicely even in the event of a US or western economic slowdown, this underpinning to the gold price was viewed as likely to continue in the coming months.

The inverse to fabrication was also seen for supply from scrap, with this falling by over 170 tonnes in the first half. Much was again due to lower price volatility. Interestingly, GFMS do not expect much undermining of the rally from this source as it is believed that the price would have to move substantially higher for scrap to rise as much of the loosely held near market supplies have already emerged, with, for example, the bulk of tired, slow selling western retail jewellery stocks having been melted down last year.

The statistical highlights of the report are outlined overleaf:

Supply Highlights

- First half **mine production** grew by 3% to 1,201 tonnes. The largest increases came from Asia, with Indonesian output growing by over 80% and Chinese production gaining nearly 20 tonnes. In contrast, Peruvian output fell back by 24 tonnes, while the South African figure was some 7% lower. Full year 2007 production is forecast to remain higher, despite a small dip in the second half.

- Global **cash costs** rose by just over 20% year-on-year in the first half of 2007 to an average of US $371/oz. Australia recorded the largest increase, though this was partly just the result of currency effects, while South Africa saw a modest increase of only 7%.

- Net **official sector** sales in the first six months of 2007 grew a modest 4% year-on-year. The gain was slight as a rise of nearly a quarter in sales by signatories to the Central Bank Gold Agreement (CBGA) was largely offset by the slump in net sales outside the group. Second half sales are forecast to more than double year-on-year to around 280 tonnes, largely through higher CBGA sales.

- **Scrap supply** fell by 28% year-on-year in the first half to just over 450 tonnes. The largest falls were recorded in the Middle East, largely as a result of comparative price stability, while the decline for India was relatively modest at 'only' 17%.

- Largely driven by widespread liquidations in the second quarter (chiefly by short-term speculative players), the first half of 2007 saw a dramatic swing to **implied net disinvestment** of just over 210 tonnes from the net *in*vestment of nearly 280 tonnes in the first half last year. Net investment, however, is forecast to return for the second half of 2007, mainly in the fourth quarter.

Demand Highlights

- Largely as a result of a drop in price volatility, **jewellery fabrication** grew by a robust 240 tonnes or 23% year-on-year and, in terms **excluding scrap**, the increase was yet greater at 46%. India accounted for more than 70% of the rise in jewellery demand, while East Asia and the Middle East also saw sizeable gains. The second half could also see a further increase though that will depend strongly on the scale and timing of any gold price rally. **Other fabrication** rose by 7% in the first half, chiefly due to higher Indian medal & imitation coin offtake. Electronics and other industrial & decorative fabrication also grew, while dental demand fell.

- **Producer de-hedging** in the first half surged to record levels just over 300 tonnes (in delta-adjusted terms), leaving producers' outstanding positions, as at end-June, at their lowest level since 1995. Second half de-hedging is expected to fall to a far more subdued level of around 80 tonnes.

- **Bar hoarding** grew by almost 80% year-on-year in the first half to over 150 tonnes, largely due to gains in India and then Vietnam, while **official coin** demand declined by 11%. This left World Investment - the sum of bar hoarding, official coins and the implied (dis)investment figure - at just 10 tonnes, its lowest level since the second half of 2000.

About Gold Survey 2007 - Update 1: In just 40 pages, *Update 1* identifies the most important economic, sociopolitical and market-specific issues facing the gold market. The publication can be ordered from GFMS for £215 or US$395 / €325 per copy. For orders and to receive further product information please contact Ms L. Perrard on: Tel: +44 (0)20 7478 1777, Fax: +44 (0)20 7478 1779, Email: sales@gfms.co.uk, Web Site: www.gfms.co.uk, Online Shop: http://shop.gfms.co.uk

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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.

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