



Publication of *Gold Survey 2008 - Update 1*

Gold Prices to Rebound after Recent Bouts of Selling as Investors Return and through a Decent Fundamental Footing but Fresh Highs Unlikely in 2008

GFMS released *Gold Survey 2008 - 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.

The fact that strength should return for the gold price after its hefty sell off since July was a key theme to the presentation. For example, GFMS believe that the recent dollar recovery is an ill founded temporary phenomenon. They cite such factors as rising US unemployment, possible slips in confidence in the US government's creditworthiness and the realisation that there may well be little, if any, narrowing this year of the US:Eurozone interest rate spread as drivers that could readily undermine the dollar. Klapwijk also commented, "I'd be far from surprised if we see a further bank failure or two in the next few months. Add that to an unwinding of dollar gains and you should see gold back over \$900, and maybe \$950".

However, the consultancy feels it has become unlikely that the record high, mid-March's \$1,011.25, is going to be broken this year. Klapwijk added, "there was an element of 'the perfect storm' to the first quarter. Not only did we see the slashing of US interest rates but there was also the surge in oil prices, falling equity markets and massive write-offs by the banks - not forgetting Bear Stearns' collapse either. And it's difficult to see all that coming together in quite the same way in the next few months".

The developments mentioned above form the backbone of GFMS' explanation of why the price posted such strong investor led gains earlier this year. Other factors considered important to the pick up in investor interest included the general rise in commodity prices, the broadening of the investor base, inflation concerns and the perception of a likely loosening of many countries' monetary policies. In turn, the periodic liquidations seen after the March high, the consultancy feels were attributable, not just to the end to dollar weakness and its subsequent recovery, but also to a need to remove some 'froth' from an overbought market, the retreat in the oil price and signs that the US economy might not be the first or most likely to suffer from a full blown recession.

While investor activity might be the prime determinant of price behaviour, the report also highlights how the fundamentals shaped the market so far this year and how they could do so moving forward. The heavy fall in central bank selling in the first half, for example, was seen as another supportive factor and one helping explain why the price did not continue falling after the initial bout of investor selling. Klapwijk added, "we're expecting central bank selling to fall yet further in the second half. That should not only provide direct support but also reassure longer term investors. Don't forget, it's largely just the short term players that have bailed out to-date".

Supply in general was deemed supportive. Scrap, for example, whilst growing, failed to get close to the record set in the first half of 2006 as a result of some people holding off from selling as they expected prices to trend higher and with much of the loosely held stocks having already emerged on to the market. The latter also helps explain why the consultancy feel that one would have to see prices sustained at over \$950, if not \$1,000, for a noticeable pick up in scrap to occur. As for mine production, this was reported to have fallen in the first half, somewhat unexpectedly, as a result of such developments as power shortages in South Africa, lower grades in Australia and unscheduled shutdowns in the United States.

Producer activity was also thought important on the demand side as de-hedging remained at elevated levels, higher than envisaged at the start of the year, despite the massive cut over earlier years in the producer hedge book. Nonetheless, the report does caution that, moving forward, the market could "sorely miss" the support from de-hedging, as it is forecast far lower in the second half of the year. The last main area of demand, jewellery fabrication, was reported as having fallen heavily in the first half, chiefly in response to high and volatile prices. However, the third quarter was said to have seen a rebound, with Klapwijk adding, "as soon as prices got down to around the \$800 level, offtake in price sensitive countries like India and Turkey came back very strongly. And that helps explain why we've had a few days of the gold price going sideways even when the dollar was still climbing. Of course, it's difficult to be that optimistic for jewellery looking ahead given a possible price rally at the time of a global economic slowdown".

The statistical highlights of the Update can be found overleaf.





Supply Highlights

- **Mine production** fell by over 70 tonnes year-on-year in the first half. Much was attributable to output more than halving in Indonesia, although many of the majors, such as South Africa, Australia, the United States and Canada, also posted heavy losses. In contrast, growth for world number one, China, continued, if more slowly than recently, and new projects raised output in Russia.
- Producer **cash costs** rose 20% in the first half, as a result of such factors as higher labour charges and energy costs.
- First half net **official sector sales** fell by just over a quarter. This was chiefly due to lower sales by countries in the Central Bank Gold Agreement - mainly higher Swiss releases not offsetting the disappearance of Spain as a seller. Net sales by banks outside the Agreement reached just seven tonnes. Central bank lending again fell due to low leasing rates and counterparty risk concerns.
- Higher gold prices fed through to a surge in **scrap** in the first half of 25%. The largest gain was in the Middle East, while sizeable increases were also seen in East Asia and India. The world total, however, was still down on the record set in the first half of 2006.

Demand Highlights

- **Jewellery demand** in the first half slumped by almost a quarter (and in terms excluding scrap by more than a third). The key driver was the price, both its record highs and volatility, as suggested by the fact that India accounted for over 60% of the gross decline. Most other regions also saw hefty losses, with price again the chief driver although worsening economic prospects were also important. This was particularly significant for the slump in US jewellery consumption, a change which also hit fabrication in Italy and the East Asian exporters. China's robust economy meant it bucked the trend and saw demand growth, as did Russia and Egypt. The 12% drop for **other fabrication** in the first half was mainly due to the slump for medals & imitation coins, although all its remaining components (electronics, official coins, dentistry and decorative) also fell.
- There was a marked swing to a first half **implied net investment** figure of over 200 tonnes from implied disinvestment of nearly 180 tonnes last year, despite the dramatic liquidation that occurred in the second half of March. In contrast, **bar hoarding** fell by around 10%, chiefly as price damage in India and intensified Japanese dishoarding outweighed gains in Vietnam and China. Nonetheless, World Investment (the sum of the implied figure, coin demand and bar hoarding) in the first half was up nine-fold year-on-year, thanks to the hefty swing for implied investment.
- Net producer **de-hedging** in the first half remained strong, and far higher than expected, at over 250 tonnes. Most activity was down to the two companies with the largest hedge books, AngloGold Ashanti and Barrick Gold. The first half saw a surprisingly low level of fresh hedging given the highly advantageous prices as investors/producers retained a staunch anti-hedging sentiment.

© Copyright GFMS Limited - September 2008.

Whilst every effort has been made to ensure the accuracy of the information in this document, GFMS Ltd cannot guarantee such accuracy. Furthermore, the material contained herewith has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient or organisation. It is published solely for informational purposes and is not to be construed as a solicitation or an offer to buy or sell any commodities, securities or related financial instruments. No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein. GFMS Ltd does not accept responsibility for any losses or damages arising directly, or indirectly, from the use of this document.

Gold Survey 2008 - 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 £250 or US\$460 / €350 per copy. For orders and to receive further product information please contact Elena Patimova - Tel: +44 (0)20 7478 1750, Fax: +44 (0)20 7478 1779, Email: sales@gfms.co.uk, Web Site: www.gfms.co.uk, Online Shop: <http://shop.gfms.co.uk>

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