



Publication of *Gold Survey 2006 - Update 2*

Rally in Gold Price Forecast for First Half 2007 due to Growth of Investor Interest

GFMS released *Gold Survey 2006 - Update 2* today, their latest report on the gold market. A summary of the findings of *Update 2* was given by Paul Walker, CEO of GFMS, at a seminar in Toronto organised by the precious metals consultancy.

The outlook for the price is a key element to *Update 2* and this the consultancy believes should track higher over the coming months. As Walker noted, "we should be seeing prices getting in the \$670s in the first half, although it is less certain we will see the recent high of \$725 surpassed. That could still occur, maybe further into the year or possibly in 2008, especially if the situation in the Middle East deteriorates significantly, driving oil prices higher."

GFMS therefore believe it is investment that would be the prime driver of any such rally. Walker commented, "we're fully expecting investor buying to come back in force, mainly in response to actual and potential dollar weakness. A slowdown in the US economy and disappointing returns in conventional assets, such as equities, should also lift gold."

Update 2 also sees little threat from stop loss selling or profit taking, with the main supply and demand fundamentals providing the gold market with a firm underside. Looking firstly at jewellery demand, the consultancy noted that this proved very weak in the first half of 2006, chiefly as a result of the second quarter price spike, but came back fairly confidently in the second half as pent up offtake responded well to lower volatility, with buyers emerging on any price dip.

A similar performance was expected this year, with Walker adding, "we've just seen the market hold above the \$600 level, even though we saw the dollar:euro strengthen to \$1.29, and physical buyers no doubt explain a big part of this resilience." The consultancy ascribe this robustness to such factors as the buoyancy of economic growth in countries like India or China.

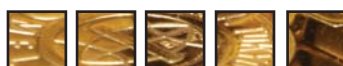
The other two significant price supports concern official sector sales and old scrap. Looking first at the central banks, GFMS estimate that their sales halved in 2006 and are likely to remain subdued in 2007, on both occasions due to signatories to the Central Bank Gold Agreement (CBGA) significantly underselling their quota and to occasional purchases outside of Europe (though the latter do not as yet include any expectations of purchases by the dollar-rich East Asians).

Turning to old scrap and GFMS estimate this to have risen by around a fifth in 2006, mainly in the first half and largely in response to the price, but this is expected to fall by around one-fifth year-on-year in the first half of 2007. By way of explanation Walker commented, "you would need a price well into the high \$600s to see any sizeable pick up in scrap. Much of the loosely held jewellery was shaken out during the April/May price spike last year and people have come to see \$600-\$650 as quite ordinary levels."

The only two negatives for the price noted in *Update 2* concerned mine output and producer de-hedging. There was some price support from mine production in 2006, which came in lower than forecast with a 2% fall, but GFMS expect to see a modest rise in 2007, largely as new projects come on stream or ramp up to full capacity.

De-hedging was thought to have been an important factor behind initial price strength last year, as the Barrick buy-back lifted the first half 2006 total to almost 300 tonnes, but overall de-hedging is expected to return to a more normal rate of under 200 tonnes a year in 2007, unless fresh corporate activity brings about another shock. The report notes, though, that there is little evidence of interest in non-project hedging, despite the widening contango.

The statistical highlights of the report are outlined overleaf:





Statistical Highlights:

Supply

- **Mine production** in 2006 fell by 2% to 2,467 tonnes, a figure slightly lower than once expected. Marked losses were seen for the three largest producers (South Africa, Australia and the United States) and Indonesia. In contrast, gains were achieved in China and many countries in Latin America and Africa. First half 2007 output is forecast to show modest year-on-year growth.
- Weighted average **cash costs** rose in all major regions for the nine months to September, with the global figure up 13% year-on-year. This was primarily caused by higher input costs in such areas as diesel fuel, steel, cement and mining reagents.
- Net **official sector sales** in 2006 are estimated to have halved to 330 tonnes. The decline was driven by lower sales from signatories to the second CBGA coupled by countries outside the Agreement featuring as modest net purchasers. Net sales in the first half of this year should fall year-on-year as CBGA sales remain subdued and small scale extra-European purchases continue.
- **Scrap supply** last year rose by a fifth, with much of the growth occurring in the first half and largely in response to the gold rally. The Middle East and then Europe saw the largest gains, while in sharp contrast Indian scrap actually fell.

Demand

- **Jewellery fabrication** slumped by over 400 tonnes in 2006, chiefly in response to higher and more volatile prices, with much of the decline taking place in the first half. In terms **excluding scrap**, the fall last year was more severe, with the first half down more than 40%. Losses were greatest for the price sensitive regions of India and the Middle East, though substantial losses were also recorded in Italy and East Asia excluding China. This sector is only forecast to show a slight retreat in the first half of 2007. **Other fabrication** grew by over 10% in 2006, chiefly through higher coin and electronics demand.
- Net **producer de-hedging** last year proved far stronger than anticipated at a provisional total of just over 400 tonnes (or more than four times volumes in 2005). This surge was largely due to the buy-back of Placer Dome's hedge position by Barrick following its acquisition of the former. De-hedging this year is expected to return to a more 'normal' run rate of slightly under 200 tonnes.
- **Implied net investment** fell by around a quarter in 2006, not so much due to a fall in investor interest but to the emergence of two-way activity in the market. There was a notable shift in business from the exchanges to the over-the-counter markets. As regards the other types of investment, **bar hoarding** eased to just under 230 tonnes, mainly through a slump in Japan outweighing gains in India and Vietnam, while **official coin** sales saw growth of 15%. This put World Investment (the sum of the implied figure, bar hoarding and coins) last year at just over 680 tonnes, or down 16%. The chief development forecast for World Investment in the first half of 2007 is a surge (versus the second half of 2006) in implied net investment.

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Gold Survey 2006 - Update 2 Gold Survey Update 2, published in January, provides a thorough and comprehensive interim analysis of the most recent developments in the gold market. In just 40 pages, Update 2 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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