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Gold – Investment Demand Stampedes

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On December 17th 2008 the combined gold holdings of the World Gold Council gold Exchange Traded Funds and Barclays Gold Trust stood at 985.59 tonnes. By the 16th January 2009 this had risen to 1009.92. By 30th January early in London time they had grown to 1079.83 a growth of almost 70 tonnes in two weeks. To give one perspective, the Central Bank Gold Agreement signatories [European central banks only] sold only 3.5 tonnes in the last two weeks. There are many other gold bullion-holding funds in the developed world from Canada to Switzerland that are not included in this total. If they were the total would be approaching 1200+ tonnes. Clearly we are seeing a stampede of institutional fund management into gold at present!

Gold Exchange Traded Funds

The world Gold Council gold Exchange Traded funds cover the U.S.A., the United Kingdom and the Eurozone, plus Australia and South Africa. They also attract shareholders from other parts of the world who access these shares in those countries from outside. These funds are next only to owning gold bullion and coin itself, the ultimate way to own gold. As a reflection of global developed nations investment demand they are limited, because traditionally investors in the developed world held gold bullion and coin directly. In addition, these funds exclude demand from the Indian sub-continent, the most important source of investment demand and from Asia, where gold markets are not sufficiently developed to quantify investment demand accurately.

The New Way for Institutional Funds to Buy Gold

Perhaps the most significant feature of gold Exchange Traded Funds is that they have only been around for a couple of years. The perceived joy of these funds is that each share in them represents a portion of gold itself, which these funds buy as the shares are bought. As the shares are sold, so the fund administrators sell equivalent amounts of gold. Not only does this make the holding of gold much cheaper and easier to deal in their formation opened up an entirely new type of investor, who was previously barred from entering the gold market directly. This type of Investor has the capacity to be by far the largest holder of gold ever seen. With global pension fund assets estimated at \$18.6 trillion by the end of 2005 only a tiny proportion of that amount has entered the gold Exchange Traded Fund market so far. Bear in mind that at \$900 an ounce, one tonne of gold costs \$29 million, so far. So the 1200 tonnes held in this manner represent only \$34.8 billion or 0.19% of these pension funds assets [there are many other types of funds other than Pension Funds as well]. Quite a way to go before gold makes a dent on these portfolios.

Institutional Funds were barred from holding gold itself across the world. At best they would own shares in the mining companies that produced gold. In doing so they added to their holdings corporate risk, a feature many would have liked to avoid. Their arrival on the stock exchanges of the developed world signaled a way to lower such risks and 'own' gold itself via these shares. Initially the small size of these funds restrained the larger funds from participating, worried as ever about the liquidity of the shares in these funds. Over time the demand for these shares grew alongside their ability to serve the community as an effective alternative to gold itself. Perhaps the greatest task of the World Gold Council was to educate fund managers in the joys of such shares. It appears their work has borne fruit. Now a fund manager not aware of such an alternative to gold shares is thought of as deficient. The gold Exchange Traded Fund shares are now the global institutional way into gold.

Central Banks in the Gold Market

The Central Banks of the world are the largest holders of gold in themselves, despite that unquantifiable fact that around 20,000 tonnes of gold are held privately across the Indian sub-continent. So as to give us a sense of proportion on the top cats in the neighborhood, here are the current gold holdings of the top 9 central banks in the world.

Central Bank Gold Holding in 2008

Gold (Tonnes)*	
United States	8133.5
Germany	3417.4
IMF	3217.3
France	2568.3
Italy	2451.8
Switzerland	1113.2
Japan	765.2
Netherlands	621.4
China	600.0

If we are to take the entire privately held gold Exchange Traded Fund shares they would represent more gold than held by the Swiss National Bank, Switzerland's central bank. Japan was overtaken a long time ago. Take the world Council gold Exchange Traded Funds and the Gold Trust totals and at the present level of demand the next fortnight will see them overtake Switzerland alone.

New Investors in Gold Exchange Traded Funds?

Why is size important in this context? Many fund managers have been eyeing these funds with caution, waiting for them to 'mature' as investment vehicles. With the above figures their maturity is without question. Consequently the largest of investment funds from all sides of the investment spectrum will regard these vehicles with respect and invest in gold through them.

The present global economic climate, fraught with uncertainty, fear and currently a savage gauntlet for fund managers is making gold a desirable alternative and counter to such investments. Fund manager after fund manager is weighing the wisdom of holding gold in portfolios as a result. Consequently as the 2009 prospects for the global economy point to deflation of frightening proportions followed likely by explosive inflation as the Tsunami of newly printed money from all parts of the globe hits it, gold has moved to center stage as an investment of note.

It is likely then that these investment vehicles will be at the vanguard of fund management in gold in the years to come.

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