

What Happened in the London Gold Market during the Gold Standard: 1925-1931

BY FERGAL O'CONNOR, LECTURER IN FINANCE, CORK UNIVERSITY BUSINESS SCHOOL

As part of LBMA's plans to commemorate the centenary of the first gold price on 12 September, 1919, we feature here the second of Fergal's four *Alchemist* articles which look back at the history of the gold price.

April 1925 marked a return to the Gold Standard for Britain after six years of floating gold prices. The London gold price auction had been revitalised through the efforts of the Bank of England in 1919, with this as a primary goal, but its reintroduction proved to be a double-edged sword for the London gold market during this period.

APRIL 1925 MARKED A RETURN TO THE GOLD STANDARD FOR BRITAIN AFTER SIX YEARS OF FLOATING GOLD PRICES.

While gold prices floated freely from 1919 to 1925, most of the gold trading in London was transacted through the Gold Fixing, with what remained going through London's OTC gold market. But with the return to the Gold Standard, most newly mined gold shipped to London was sold directly to the Bank of England, bypassing the Fixing.

This meant that the Bank now set what was seen as the 'Official Gold Price' for the London market, as the Fixing had for the previous six years (Harvey 2008). In addition to this, the agreement between the Bank of England and the South African gold producers to sell all their gold through London was

weakening and some of this gold was now being shipped directly from Durban to India and other destinations (Ally 1994).

While all gold trading in London was now taking place through the Fixing, with no OTC market operating, the above factors led to a drop in liquidity within the Fixing. Its reduced importance in setting the gold price led to the daily price from the Fixing being referred to as the 'market price'.

SUPPLY CHAIN ISSUES

Until June 1930, gold had traded in a tight range between £4.2479¹ which was the Bank's official price, and £4.2406. The Gold Fixing did start to see unexpected price changes from mid-1930 and even though the maximum price of old gold was supposed to be that set by the Bank, it spent a good period of time above that. This stemmed from an issue in the supply chain of fine bar gold.

As the Gold Standard started to weaken, purchases of gold by the Bank of France increased dramatically in 1929 and a discrepancy in the fineness of gold between the two countries led to specific shortages. The London market had moved to a 99.5% pure basis in

1919 with the commencement of the Fixing, in order to come into line with other major markets. However, the purity of the majority of bar golds in London's vaults remained at the historical norm of 11/12th fine.

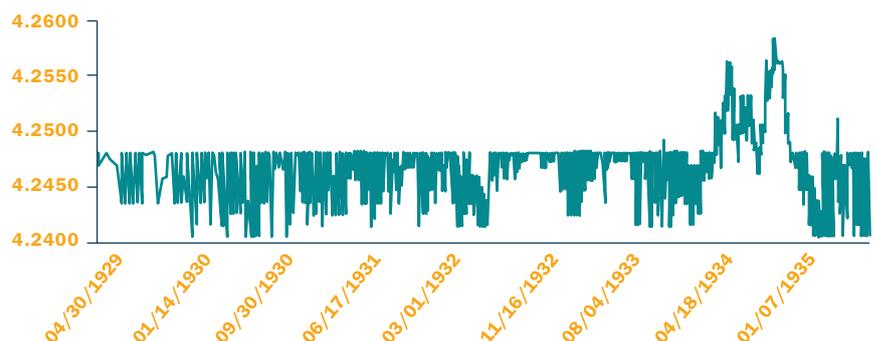
Quantities of gold delivered through the Fixing were normally adjusted for this so that the gold stock in London did not need to be refined to a higher purity.

But the Bank of France refused to accept delivery of the lower-purity bars and this created a sudden increase in demand for any 99.5% bars that were available, while refiners scrambled to refine the standard bars to the required higher purity.

By September, the Bank of England could only secure gold on the open market by paying a price above £4.2479 (Samuel Montagu and Co. 1931).

This episode of higher prices came to a close on 15 January 1930, when the Bank of France changed its policy and accepted the lower fineness, resulting in the quantity of gold being shipped to France increasing dramatically as London's limited refining capacity no longer constrained supply (Samuel Montagu and Co. 1932).

GOLD FIXINGS PRICE, £s MODERN: 1925-1931



1. Prices on the London Market at this time were quoted in pounds, shillings and pence, all figures referenced here are quoted in modern decimalised pounds sterling.



Fergal O'Connor is a lecturer in Finance at Cork University Business School and was previously a lecturer at the University of York. His

research on Precious Metals began when he was awarded the 2011 LBMA PhD Bursary for the study of the London Gold Market and he has gone on to publish a range of research on the topic. Currently, his research focuses on building a clear picture of the operation of London Bullion Market from its inception in 1919, as well as a daily price series for gold and silver.

THE END (AGAIN) OF THE GOLD STANDARD

On 20 September 1931, the Treasury announced that it had advised Britain to depart the Gold Standard (UK Government, 1932) and a bill was debated on Monday 21 September at 4pm (FT, 1932). However, on the morning of 21 September, before the vote, gold fell in value from £4.2479 to £4.2406 per fine troy ounce.

As it was generally accepted that Britain would depart the Gold Standard, and this would result in an increase in the sterling gold price, at first glance, this

seems peculiar. Who would sell at the lower price knowing it would increase the following day? The price that was fixed on the morning after the vote was £4.9792 – a rise of over 17%. By the end of the week, the gold price was fixed at £5.7375 – a rise of over 27%.

The fall in price on the day of the vote seems to have been due to the fact that the value quoted was marked as 'Nom', which indicates a day when no trading took place on the Fixing. The published price for that day would have been the US dollar gold price converted into sterling at that day's exchange rate, as determined by NM Rothschild & Sons.

The price on 22 September was also Nom, indicating that gold trading did not recommence until 23 September, when the gold price fixed at £5 per fine troy ounce.

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pure basis in 1919 with the commencement of the Fixing, in order to come into line with other major markets.

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Samuel Montagu and Co. 1931. *Annual Bullion Letter 1930*.

Samuel Montagu and Co. 1932. *Annual Bullion Letter 1931*.

2019 CENTENARY OF THE FIRST LONDON GOLD PRICE

100

GOLD PRICE CENTENARY

BY AELRED CONNELLY, PR OFFICER, LBMA

In the last edition of the *Alchemist* we looked back at the history of the gold price and now we give a nod to the present and to the future.

Today, the LBMA Gold Price continues to be set in London and remains the international benchmark price for the gold market. Since IBA became the independent administrator in 2015 the number of direct participants has grown from 5 to 15, including three Chinese banks. And the number and global reach continues to grow, with Marex Financial Limited the latest participant to join on 3 April, 2019. We look forward to more participants joining as we look forward to the next 100 years.

The gold price has survived turbulent times during the course of the last 100 years. Through its continued recognition as a globally established benchmark, we celebrate the courage of the gold market in its ability to seek out hope, and to adapt. LBMA looks forward with anticipation to the ways in which the market will continue to evolve and grow over the next 100 years.



WHAT'S PLANNED FOR 2019?



SEMINAR & COCKTAIL RECEPTION, 12 SEPTEMBER

To be held on the centenary of the first gold price and held in the current Rothschild building which was built on the site of (the second) New Court, St Swithin's Lane, where the first gold price was set. We are grateful to NM Rothschild for their support in co-hosting this event with LBMA.



GOLD TALK, 27 SEPTEMBER

Ruth Crowell, LBMA CEO and Paul Fisher LBMA Chairman, will deliver a joint talk at the Bank of England on the gold market.



SEMINAR & GALA DINNER, 3 DECEMBER 2019

Will take place in the historic surroundings of the Goldsmiths Hall in the heart of the City of London. We would like to thank the Goldsmiths Company for their support in hosting this event.



COIN COMPETITION

LBMA Members, Associates and GDL refiners have been invited to take part in a competition to design a silver 1oz medallion to commemorate the centenary. Designs will be judged by an independent panel of industry experts.



UPDATING THE ROTHSCHILD'S CHART CELEBRATING THE 80TH ANNIVERSARY OF THE PRICE

With the assistance of Rothschilds, we will be looking to update the chart that was produced by Rothschilds to mark the 80th anniversary of the Gold Price back in 1999.