GORDON'S BROWN BOTTOM, 20 YEARS ON

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Image: Brown and Blair taken at the Labour Party Conference 1999

July 2019 marks 20 years since the UK began its infamous gold auctions, more than halving the nation's gold reserves inside three years. The decision and its timing – announced two months in advance – knocked prices 10% lower before the first sale began, on 6 July. Why would a seller want to do that? And if the Bank of England was selling, on orders from No.11 Downing Street, who on earth wouldn't?

BACKGROUND

"Conspiracy theories are widely circulating in the City," said Conservative MP Peter Tapsell to Parliament in June 1999, berating the New Labour government for planning to sell three-fifths of the UK's 715-tonne holdings. Internet chatrooms also lit up with rumours that "famous foreign finance houses" were heavily short, bribing their old Oxford college friends (now at the Treasury) to kill any price rise. Analysts, in these very pages, said Chancellor Gordon Brown was in fact rushing to sell before he took Britain into the new euro currency without asking voters.

MORE THAN 1/5 OF THE UK TREASURY'S OWN GOLD WAS OUT ON LOAN

HEDGING AND SHORT-SELLING

The Bank of England's then Head of Foreign Exchange, Clifford Smout, denied any conspiracy "with persons known or unknown!", in an article here in *The Alchemist,* but the sales still looked "catastrophic" to tabloid front pages, "bloody unhelpful" to gold-mining bosses, "appalling" to most London dealers and horrific to reserve managers across the Channel. Yet, if there had been a conspiracy to kill gold, each of these groups would have been implicated.

Borrowing gold in London, lent by European central banks seeking a yield, helped "scapegoated funds and lamented mines to stave off closure" throughout the 1990s, as Andy Smith (then at UBS) noted. Hedged by borrowing and selling well over one year's full output, global mine production set a run of new records even as prices kept falling. But central banks as a group had lent out half as much again, giving speculators perhaps 1,500 tonnes to play with. Indeed, more than a fifth of the UK Treasury's own gold was out on loan in 1999, according to BoE data, potentially helping short sellers front-run July's sale after the UK Government's announcement on Friday, 7 May. As for the financial press, Brown's move just confirmed their disdain for bullion.

"The death of gold" had in fact been splashed across the *Financial Times* 18 months earlier, back when the BoE's then Governor Eddie George mused how – what with Belgium, Canada and the Netherlands selling 1,590 tonnes between them since 1990, and Argentina plus Australia selling 290 tonnes in 1997 alone – the new European Central Bank might not bother keeping any bullion from the 11 founders of the forthcoming single euro currency. The ECB eventually decided to keep 15% of its members' subscriptions in gold, but that left half their aggregate hoard of 12,500 tonnes unneeded.

RUSH FOR THE EXITS

April 1999 then saw prices sink to near two-decade lows when Switzerland, the fifth-largest holder of gold, narrowly passed a referendum revoking the franc's role as the last gold-backed currency, green-lighting the sale of 1,300 tonnes. The next week, the International Monetary Fund joined the queue, "practically unanimous" in backing calls (led by Gordon Brown) to cut the world's third-largest holdings and write off Third World debt for the Millennium.

1. Note manufactured products such as jewellery come under a different chapter heading (7113, for example).

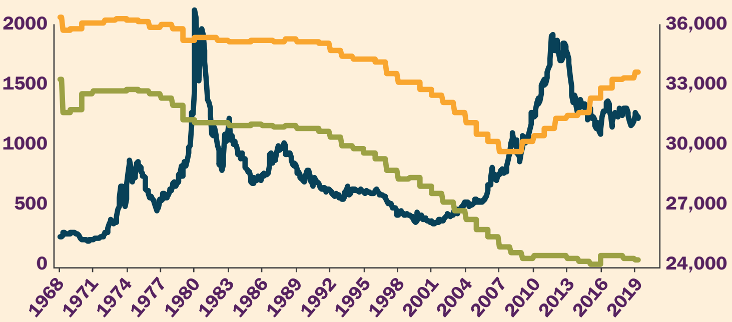
Ten days later, the UK Treasury stunned the market with its plan to "better balance" Britain's foreign exchange portfolio, selling 55% of its gold to buy more dollars, euros and yen for its Exchange Equalisation Account.

KEN CLARKE WANTED TO MAKE THE SAME ERROR BUT GAVE UP IN THE FACE OF BANK OF ENGLAND STALLING

Coming from the nation that had "invented the gold standard", as consultancy Virtual Metals put it, the news sent gold down to 18 fresh 20-year lows inside three months, costing the EEA nearly $43 million on the first 50 tonnes sold; versus 1999's average price before the announcement. Posterity hasn't recorded who coined the phrase "Brown Bottom" (sometime before 2007, according to Google), but 20 years ago this summer, it applied more to market participants than to gold's then tumbling price. Because, as Kamal Naqvi (then at Macquarie Equities) told the FT: "The ultra negative view is justifiable; the British are looking to sell before everyone else."

Gordon Brown at least managed to achieve that (see Figure 1). Hindsight also says that selling gold near its cheapest real prices in history probably wasn't his worst policy mistake as New Labour's "prudent" Chancellor. (Conservative predecessor Ken Clarke wanted to make the same error, but has said he gave up in the face of Bank of England stalling.) Brown's raid on dividend tax credits permanently reduced the nation's private pension provision. Dismantling City oversight by the Bank of England, and instead imposing a new, complex and wholly inadequate regulatory regime, also runs close as does his support for Tony Blair's disastrous war in Iraq. But either way, the gold sales decision and timing look wilful, if not vindictive.

FIGURE 1: OFFICIAL GOLD HOLDINGS VS. REAL PRICE



Gold adjusted for inflation to 2019 dollars per ounce (left axis)
Developed West + IMF,BIS, ECB (tonnes, right axis)
Total reported worldwide (tonnes, right axis)

Source: BullionVault via WGC, LBMA, St.Louis Fed

GOLD VS GREENSPAN

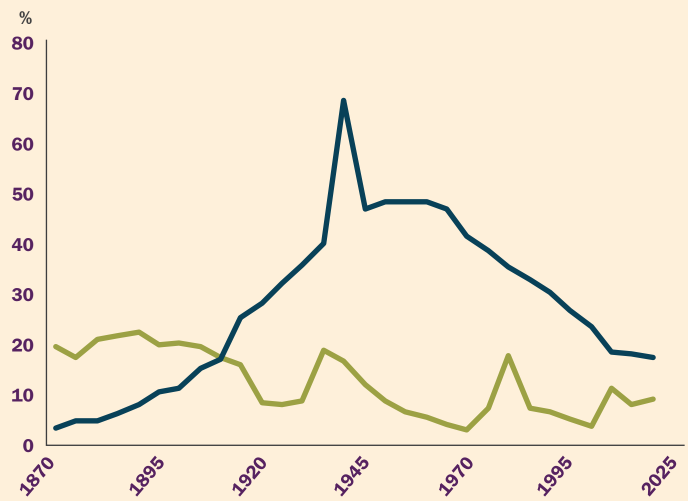
Unnamed sources have long told the press that the Treasury's move was strongly opposed by the BoE. In public, the Old Lady would only note coldly that it was "a political decision", and her authorised biography of 2017, David Kynaston's *Till Time's Last Sand*, doesn't deign to mention the affair. But what you think starts with where you sit and, at the end of the 20th century, most people outside London's bullion market could see nothing beyond a relentless decline for gold, both in purpose and price.

Not used for circulating coin since the 1930s, and cut out of the world's monetary system over the following four decades, the metal had lost 80% of its real worth from the 1980 peak, failing to beat inflation (let alone equities) and falling back to its all-time lows compared to the value of world economic activity (see Figure 1).

The technocrats who had replaced gold, in contrast, were enjoying a bull market.

"The twilight of gold makes sense," wrote Niall Ferguson in *The Cash Nexus*, his history of debt and money published in 2000. "[It] has a future," the Harvard professor (then at Oxford) went on, "but mainly as jewellery ... in parts of the world with primitive or unstable monetary and financial systems." Put another way, "Who needs gold when you've got Alan Greenspan?", as the *New York Times* asked of the US Federal Reserve's 'Maestro' just three days before the UK's historic announcement.

FIGURE 2: ALL THE GOLD ABOVE GROUND



Value as percentage of world GDP
Percentage in official-sector control

Source: BullionVault via Timothy Green, Metals Focus, various

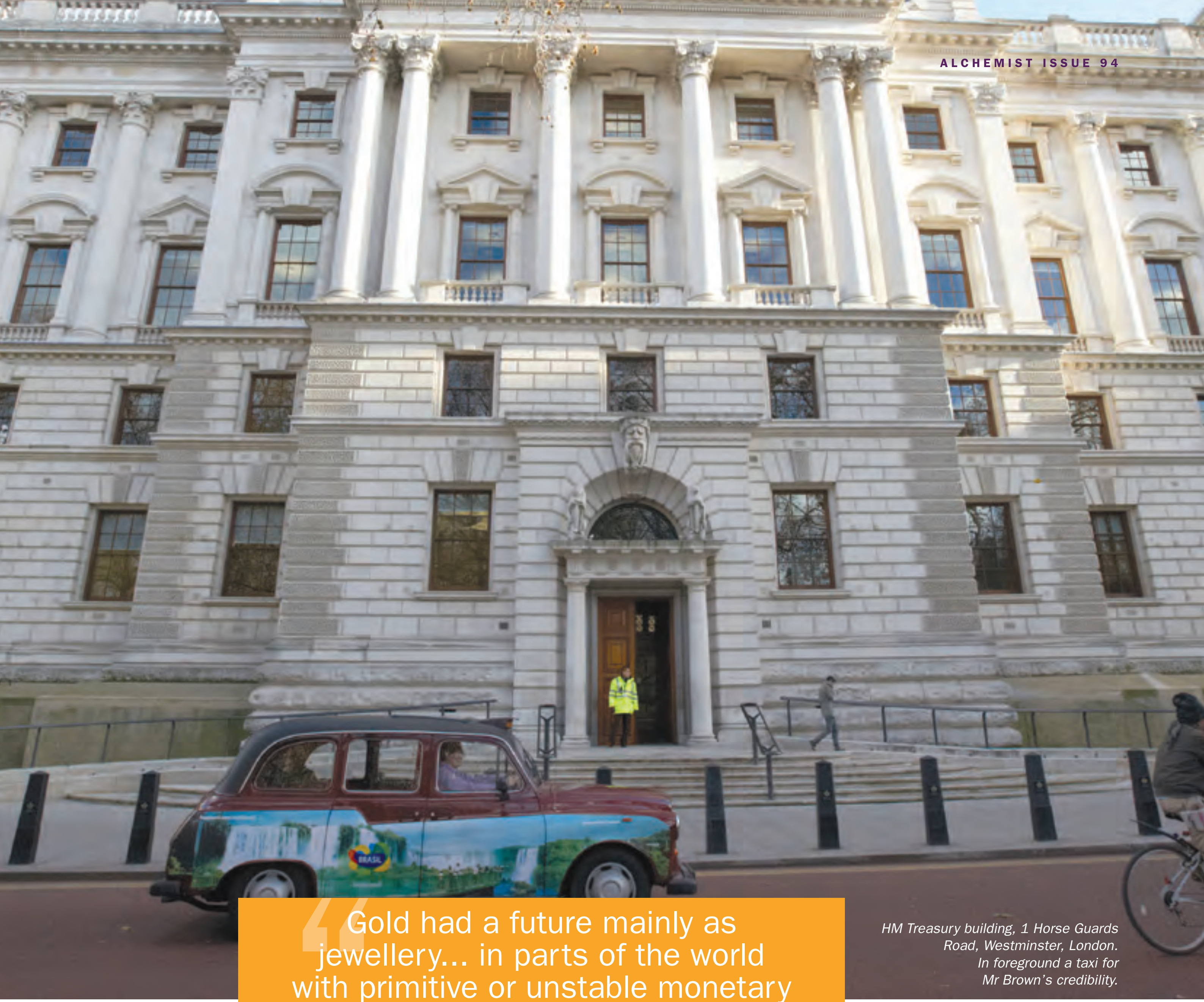
On the day itself, and amid the first tech stock bubble, New York was abuzz with the investing tip website, *TheStreet's*, forthcoming float. To get in on the deal, singer-actress Barbra Streisand reportedly chased the dotcom's CEO with free concert tickets (in 1978, her friend Bette Midler had apparently demanded payment for a tour in gold krugerrands); the stock doubled on its debut the following Tuesday.

Next to such dynamism, those unrusting bars losing value in central bank vaults looked a very "barbarous relic" as John Maynard Keynes had called gold seven decades before, railing against the rules and restrictions of the Gold Standard.

THE ULTIMATE CONSPIRACY

Glancing back at gold's dramatic revaluation of the past 20 years, it's hard not to wonder if – conspiracy of conspiracies! – Brown and his bright young team (the two Eds, Balls and Miliband) weren't themselves heavily long in spring 1999. Bullion prices rose well over five-fold in dollars, euros and yen by the peaks of 2011-2013. Against the British pound, gold today trades more than six times higher. More instantly, the Treasury's announcement proved so awful for gold prices that it brought the threat of uncontrolled central bank selling to a head, jolting the rest of Europe into adopting and adapting the same strategy of 'tell then sell' with a public agreement to cap sales for the next five years.

Announced at that September's annual IMF (and with Switzerland and the BoE among its 15 signatories), this sudden transparency so clearly reassured the market that the next morning gold made its sharpest one-day jump since 1982, starting a two-week gain of 25% that hasn't been beaten since.



HM Treasury building, 1 Horse Guards Road, Westminster, London. In foreground a taxi for Mr Brown's credibility.

> "Gold had a future mainly as jewellery... in parts of the world with primitive or unstable monetary and financial systems"

Renewed three times, a fifth Central Bank Gold Agreement shouldn't waste much time this September when the current deal expires, because any sales cap became redundant when Western selling ended amid the global financial crisis in 2009 (Figure 1). So too did any pretence of wanting to defend Western currency values or needing reserve assets to do so, replaced by bail-outs, QE money creation and near-zero to negative interest rates. Together, this has revived a strongly symbolic role for gold among the public (shown by grass-roots campaigns to "Bring home our gold!"). It has also seen a surge in emerging market nations buying gold to hedge those Western reserve currencies under attack from their own issuers.

A MISSED OPPORTUNITY

Led by Russia, China and Turkey, 30 different countries have added to their gold reserves over the last decade, of which only two are what we now call 'Western' nations (Poland and Hungary recently doubled and raised gold ten-fold repectively, but only to 10% and 4% of foreign reserves; their European Union partners average is 26%) and only one is classed as an advanced economy (South Korea). More crucially for our market, however, the "elusive investor" who GFMS's Timothy Green noted was missing throughout the 1990s has returned in force.

Coins, bars and exchange-traded trust funds backed by bullion have accounted for nearly one-third of global demand so far this decade, up from an average 19% in 2000-2009 and barely 10% in the late 1990s.

Longer term, this means that while central banking's switch to net buying has slowed the reprivatisation of gold now running since the collapse of the post-WWII Bretton Woods system, it has not yet reversed it. Official sector holdings in 1968 accounted for some 40% of all the gold ever mined in history. By 1999, that figure had fallen below 25% and it is now flattening (but still falling) at around 17% (see figure 2).

"If properly marketed, these [auctions] could act as a shop window for gold," wrote the BoE's Smout here in *The Alchemist* after the UK's 1999 announcement. Peter Fava, then chair of LBMA, also thought selling Treasury gold direct to the public would "be a great opportunity", and perhaps it could have soothed tabloid anger, because "the money raised by privatisation, while useful, has always been a second-order question", as Brown's predecessor Nigel Lawson said of the 1980s' hugely under-priced sales of state assets such as British Gas, British Telecom and council housing under Margaret Thatcher. But New Labour couldn't possibly promote the barbarous relic as a wise investment, not when Brown's economic management meant *Things Can Only Get Better* as the party kept promising by taking D:Ream's chart-topper for its conference anthem.

GOLD AND HISTORY RETURN

Alongside central banking and PR spin-doctoring, geopolitics also seemed to be nearing perfection as the 20th century drew to a close, or so Western policymakers thought after skim-reading the back of US State Department Director Francis Fukuyama's best-selling *The End of History*. The book was more nuanced than the jacket blurb, but Soviet Communism's collapse, plus China's move towards a market-based economy (albeit run by a military dictatorship), appeared to confirm that the world had "no alternative" to Anglo-American capitalism, resulting in the "end state of the historical process ... a moment in which a final, rational form of society and state became victorious".

Put into more practical terms for reserve managers, "The traditional reasons for holding gold have included the war chest argument", as the UK Treasury said in its 7 May 1999 press release. But who needed a war chest when our side kept winning? That very night, the US Air Force bombed the Chinese Embassy in Belgrade, killing three people, thanks to a failure of CIA intelligence in NATO's "humanitarian intervention" against Serbia over its policy in Kosovo.

THE CBGA'S SALES CAP BECAME REDUNDANT WHEN WESTERN SELLING ENDED AMID THE GLOBAL FINANCIAL CRISIS. SO TOO DID ANY PRETENCE OF WANTING TO DEFEND WESTERN CURRENCY VALUES.

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For investors at least, "Gold remains the cleanest insurance against such overconfidence", as SocGen analyst Dylan Grice noted 10 years after the Brown Bottom. Skip forward another 10 years, and US stock markets are again testing new all-time highs as investors pour cash into unproven ideas (83% of new US listings were loss-making companies in 2018, beating even the tech bubble's 2000 peak). As for politics, "the liberal idea is obsolete", declared President Putin of Russia, gold's heaviest nation-state buyer since the Brown Bottom, at June's G20 meeting in Osaka, Japan. With gold's no.2 buyer, China, also boldly challenging Western hegemony around the globe, the turmoil of the past 20 years suggests it's not worth trying to forecast how gold's role will adapt to the next 20 years of financial and political change.

But if gold does continue to grow its value and use among reserve assets, the Treasury's decision of 1999 will mean the UK starts the future very much in the second rank.

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