GOLD INVESTING/ HOARDING IN THE FREE 1930s LONDON MARKET: 1931-1939

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

The third instalment of Fergal's academic analysis of the gold price which focuses on the years leading up to the start of World War II.

On Sunday, 20 September 1931, the UK Treasury announced that it had advised His Majesty's Government to depart from the Gold Standard (Government, 1932). This action reinaugurated a free market for gold in London following six years on the Gold Standard. The London gold market would continue to operate (relatively) freely until 3 September 1939, as World War II broke out.

This eight-year period saw increased interest in gold from investors, with M. Eccles (1936) at the US Federal Reserve pointing to "private hoards" of gold being worth approximately $2 billion in total globally in 1936, which in today's terms would be about $483 billion based on Economic Share. The Federal Reserve (1954) further reported that between 1931 and 1954 about $21 billion of gold had been purchased by private individuals, or $1.1 trillion in terms of modern Economic Share. The total value of gold held by private investors in 2018 came to approximately $1.69 trillion based on World Gold Council estimates – indicating that investors in the 1930s held gold in similar proportion to investors today.

WHERE PREVIOUSLY ONLY ONE LINE HAD BEEN AVAILABLE BETWEEN ALL THE PARTICIPANTS EACH PARTICIPANT WAS PROVIDED WITH A PHONE

Gold ownership during this period was always referred to as 'hoarding' whether by national authorities or the bullion banks themselves. Montagu's Annual Bullion Letter in 1932 says that the London market gold price was not just set by reference to the US fixed gold price and the dollar-sterling exchange rate, but in fact, the London Fixings Gold Price frequently went above that price due to "Foreign enquiry for Hoarding".

Harvey (2008) discusses the evolution of the form of the London Gold Fixing in detail since its 1919 inception and points to the 1930s market as being the period when it began to resemble what we would think of today as the Fixing. Telephones became commonly used during the Fixing. Where previously only one line had been available between all the participants, now as speculation caused prices to change more frequently, each participant was provided with a phone in order to be able to discuss the changes with their home office.

AN INVESTOR'S VIEW OF GOLD IN THE 1930s

One major reason why I wanted to collect data from the 1930s was in order to examine whether the roles that gold plays in an investor's portfolio today (as a diversifier and a safe haven) are the same as the roles it played before 1968. It is possible that gold's current investment characteristics are a short-term phenomenon which might not continue going forward, if the conditions since 1968 were atypical. However, if gold acted in a similar way in the 1930s as it does today, this would make a strong case for gold to be included in investment portfolios going forward.

In order to assess gold's long-term investment case, I have also collected the first published daily index of equity prices for the London market, The Financial News 30 (FN30) Equity Index, which was first published in 1930. Figure 1 on page 7 shows the changes in the values of both over this period in which gold floated freely.

Gold outperformed equities significantly over the whole period for holders of both. The gold price increased 98% in total, with equity prices increasing 51%.

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.

FIGURE 1: GOLD PRICE (£ STERLING) & FN30 EQUITY INDEX

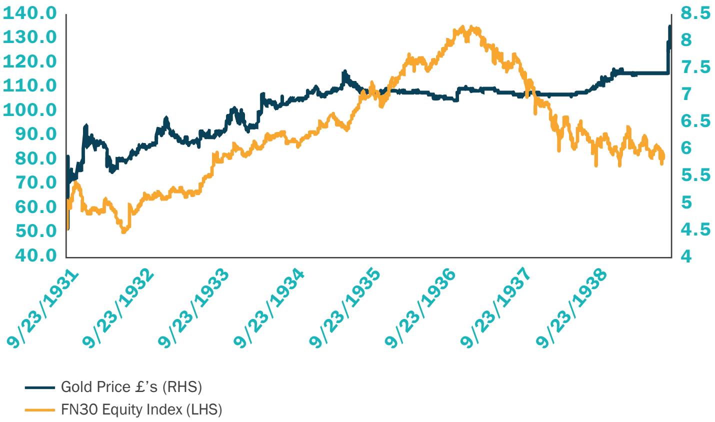

FIGURE 2: WORST DAYS ON THE LONDON STOCK MARKET

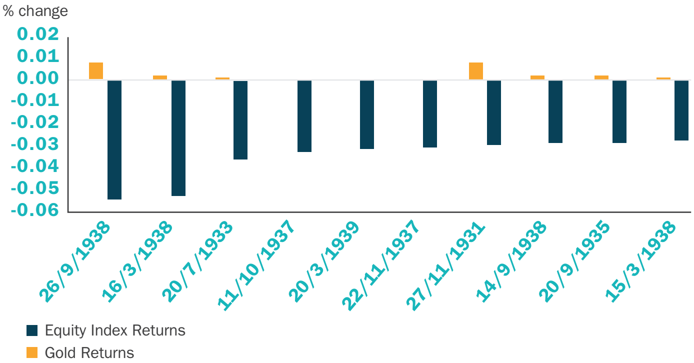

Chart above reflects the daily change in gold and stocks

As in modern markets, gold price changes had a very low correlation to changes in the value of the equity index, at about 0.21%. Gold therefore still fits well in an investor's portfolio as a diversifier.

We can also look at how the gold market reacted to sharp movements in the stock market in order to assess whether it might have been a safe haven in the 1930s. Figure 2 looks at the 10 worst days on the London equity market and what gold returns were on the same day.

On a number of these days, the gold price didn't change at all and, on every other day, gold's value increased slightly, making it exactly what investors would have looked for in a safe haven asset. If we expand our view out to the 25 worst days for equity investors, there are only two in which gold's value falls and, on both of those occasions, the Gold Fixing Price fell by less than 0.2%, while the FN30 Equity Index fell by over 2%.

The gold market of the 1930s seems to have had some similarities to the post-1968 market. More detailed research is needed, and I am currently working with colleagues on papers looking at gold as a diversifier in a portfolio of stocks and bonds during the 1930s, as well as a more detailed analysis of gold as a safe haven.

If this research is of interest please feel free to follow Fergal on Twitter at @a_fergal for updates.

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2019 CENTENARY OF THE FIRST LONDON GOLD PRICE

BY AELRED CONNELLY, PR OFFICER, LBMA

2019 marks the centenary of the first London gold price, now known as the LBMA Gold Price. In an ever changing world, it is important not only to recognise this important achievement, but to look forward to the next 100 years.

Throughout its continued recognition as the globally established benchmark, there have been significant changes to the transparency, oversight and participation in the price auction. In 2015, ICE Benchmark Administration (IBA) was appointed the first independent administrators of this regulated benchmark. Direct participation has tripled from five to 15 entities, including the addition of three Chinese banks.

To mark the centenary of the price, LBMA has arranged a series of events during 2019.

WHAT'S PLANNED FOR 2019?

SEMINAR & COCKTAIL RECEPTION, 12 SEPTEMBER

To be held on the centenary of the first gold price, in the current Rothschild & Co building, which was built on the site of (the second) New Court, St Swithin's Lane, where the first gold price was set. We would like to thank Rothschild & Co for their support in hosting this event. There will be some items from the Rothschild collection on display which will be accompanied by a talk. In addition ICE Benchmark Administration (IBA) will deliver a presentation about the gold price auction.

GOLD TALK, 27 SEPTEMBER

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

SEMINAR & GALA DINNER, 3 DECEMBER

Takes place in the historic surroundings of the Goldsmiths Hall in the heart of the City of London. A seminar will also be held earlier in the afternoon, details to follow.

COIN COMPETITION

We have received some excellent entries for the competition to design a silver 1oz medallion to commemorate the centenary. The winning entry will be judged by a panel of industry experts. The winning design will be produced in sufficient quantity as a gift for all those attending the centenary dinner in December.