

Once more unto the breach, dear friends

Editorial Comment by Tim Wilson, Managing Director, JPMorgan

There comes a time in the evolution of most products when a bold step is taken, with vision and commitment, to foster and encourage their development. Traded markets are no exception. Success for the risk-takers may not always be guaranteed, but sometimes the environment presents a set of opportunities where success is a more predictable outcome. My view is that now is the time for the London Bullion Market to look to the traded gold market in Asia for its future development.

Since the formation of the LBMA in 1987, itself a bold and noteworthy step in formalising and shaping the trading environment we all benefit from today, there have been constant discussions and efforts to refine and develop the market. The number of debates and articles about transforming the LBMA into the International BMA are too numerous to recount, but discussion has rarely been translated into action. Normally, the discussion gets sidelined by other priorities and a view that “if it ain’t broke, don’t fix it”. Well that is indeed so for the legacy business, but from my vantage point, there is a great opportunity for those bold enough to grasp it.

There are some rather well-known statistics that put this opportunity into perspective and they are worth recounting as a reminder of the direction of the market’s momentum.

Investment

- In 2009, Asia accounted for over 82% of gold bar hoarding (not just the latest craze for ETFs – but sustained personal investment in treasured assets held in personal accounts and storage facilities). India accounts for 9.5% of the world’s total gold holdings and in recent years has consumed around 25% of the world’s annual gold output, mostly for the manufacture of high-carat investment jewellery.

Production

- In 2009, gold production in Asia grew by 16%, or 91t, accounting for almost half of the global increase. Within this region, the two largest country gains were recorded in Indonesia and China. As is well known, in 2007, China took over from South Africa as the world’s biggest gold producer. It remained the largest producer in 2009 (13.3% of global production), followed by Australia (9.4% of global production). In 2009, China produced 314t of gold (up 11% on 2008). Production in China has increased by 80% in the past ten years.

Growth

- The population growth in the emerging markets is destined to have positive implications for gold demand, e.g., in Vietnam gold has a higher significance than in the Western world - the Vietnamese per capita demand is more or less on par with the German equivalent, although German per capita GDP is 40 times higher than that of Vietnam. And over 50% of the world’s population already lives in Asia, so that world economic growth are likely to be boosted by developments in Asia for generations to come.

But there is also the tangible awakening of a collective will to develop further many regional markets in Asia and there is a growing recognition that international markets should accommodate fully and meaningfully Asian time zones and practices.

“What’s the issue from an LBMA perspective?”, you may argue, after all, that London, with all its history and credibility, still sees most of the flows. After all, there is still only one true gold reference price (the London ‘fix’), while other markets trade at a differential to the fix based on grade, transport, tax and policy parameters. Again correct, but only to a point. It is no coincidence that the fastest-developing financial markets are in Asia and that most of the new commodity exchanges proposed globally are Asia-based. The operators and owners of these exchanges know, as the famous villain ‘Slick Willie Sutton’ knew, if you desire to access wealth immediately, stick close to where the money is.

JPMorgan has recently announced the opening of an LBMA-linked gold vault in Singapore – a first for the region in having a fully commercial gold vault, tied to a global trading platform, where markets will be made for loco Singapore delivery, allowing clients and the LBMA professional market full access to some of the most active financial markets in a rapidly growing region. Established in parallel with some of the great names of collectibles and valuables – amongst them Christies, whose clients continue to see compelling logic in domiciling their physical assets in havens safe from retrospective claims – we are extremely confident that our investment, although not without its challenges, will reap rewards.

Our research has shown us that investors and traders of gold (the great prudential asset) would really value trading a liquid gold market in their waking time zones, as well as having their asset safe and close to them. You just never know when you might need it... which after all, is exactly the point. Whilst the

current market has done an admirable job servicing the needs of the established investment community, there beckons a new community with a hunger and appetite for the unique investment characteristics that gold represents and presents.

At a recent investment bank flagship conference on China in Beijing, attended by some 2,000 of the world’s China active fund managers, investors and corporates, one of the keynote addresses was, for the first time, on gold. Not a coincidence. We were after all at the centre of one of the world’s great re-emerging economies, that over the past millennia has had a passion for gold and an appetite for trading it. Balancing a portfolio of sizzling Shanghai property with an investment in tradable gold, of ascertainable provenance, and complemented by access to a liquid global market for portfolio optimisation, doesn’t sound so maverick.

The LBMA has recently announced that it is negotiating with the LME in the commercialisation of its forward curve. But these Ls need not mean Limited to London. I am sure it has not gone unnoticed amongst the Asian trading community that the LME has made an unequivocal commitment to the region. “Ah, obvious for them”, you say. I would argue that it’s just as obvious for us and that some of the discussions, motivations and finally justifications that the LME used to support its decision are even more compelling for the bullion markets.

We as Market Makers and Members should be embracing the opportunity to cement our position as the pre-eminent gold trading platform, to expand and promote the benefits associated with the highly accredited, reliable and international LBMA Good Delivery List. This is no missionary zeal, this is hard-headed economics of proactively capitalising on a dominant market position. Let us not just discuss the opportunity once again, agree about the lucrative prospects and then choose to do nothing. Would it be appropriate to suggest that an Asia initiative should be one that is an agenda item on every LBMA committee, to ensure that we capitalise on our position, and derive maximum

value for our members, as well as the growing number of participants in the global bullion market?

Let us try again, one more time. ■

