

Session 5: London's Role in the Silver Market

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Thank you very much Michael for that gracious introduction, and thank you to the LBMA for inviting me to speak with you today.

The bulk of silver trading is still done in London and when thinking about speaking to you today, I went back to the *New York Times* articles and I found an article from November 1909, 100 years ago, which said: “The London silver market. The recent advance of the price of silver has attracted a good deal of attention. On March 2nd, silver for prompt delivery rose sharply. The chief cause of this remarkable movement is that the market has been deprived of supplies of silver from the Americas from which constant shipments from the Philippines has been denied. There are signs that there is indeed a corner in the market, and that April silver delivery will rise and that the shorts have been caught by forward traders from London, and that London is squeezing the market. There is also a demand from the French Mint for new coins. It is the view of the *New York Times* that New York should become the centre for world silver trading because the vast majority of ounces produced in the world are from the Americas.”

That was in 1909 and it was some journalist in New York predicting that New York would capture dominance in the silver market. I found another article in the *New York Times* of 1919, so the difference is before and after the Great War. New York, the only free silver market in the world. Large quantities of silver have been going to India recently. Silver refining is done, and production is mostly done in the Americas and precious metals are seen as a security issue for our allies. New York to take the bulk of silver trade from London.” Those predictions were made 100 and 90 years ago respectively, and they've yet to be fulfilled.

Why is London the centre for world silver trading? The decline of the Spanish empire and the eventual cessation of the Spanish

colonies helped establish London as the centre for the world silver market. The effective mobilisation of bullion has played a crucial role historically in government finances, particularly in war time, as well as in facilitating international trade and helping to make sterling the world's first reserve currency. British financial and commercial interests in Spanish America, the financing of the great mining houses and railways in North America, Australia and South Africa, and British rule in India, and similar influence in China, helped solidify London's position for the world's silver market. The London silver market was instrumental in supporting the bi-metallic monetary system, which governed the US in the 18th and 19th centuries. New York emerged as a rival to London in the early 20th century for silver

trade, but London regained its position as the world's principal silver market despite two world wars, market interruptions and disadvantages, and yet London dominates. The success of the London market lies in high-quality facilities, clearing, vaulting, personnel, legal and financial services, mine financing and standards of Good Delivery, the ability of the market to police itself, and networking. Nowhere in the world is there a single location where these services can all be provided. The overwhelming majority of silver trading is done on the OTC markets, which are cleared in London in much the same way as dollars are cleared in New York and Yen are settled in Tokyo. Silver is settled in London, much like a current or checking account at your local bank. Bullion traders from all over the world have traditionally maintained precious metals accounts with members of the LBMA. This has allowed for dealers around the world to settle bullion transactions between each other by transfers between London dealers. This puts loco London at the centre of world silver trading and the price quoted for loco London is in fact the world price for silver, i.e. it is the benchmark for silver, just as West Texas intermediate is the benchmark for world oil prices.

There are six clearing members, HSBC, a bank renowned for its ability to choose cogent and spiffy analysts, JP Morgan, Deutsche Bank, Barclays, UBS and ScotiaMocatta. The advantages of the London OTC market, compared to the futures exchanges, include such accommodations as the ability to make tailor-made agreements specifying size and delivery day and location. The first silver fixing took place in 1897 at the offices of Sharps and Wilkins. Although silver has only one fixing compared to gold, which has two, the fixing process has undeniable benefits. It is an international benchmark, it is universally recognised by dealers, banks, merchants and producers, and most producer and consumer contracts are benchmarked in loco London terms. It is a published price, which is fully disclosed publicly. It has a

narrow dealing spread due to ample liquidity and market participation, and any quantity can be accommodated. It also provides an amenity and client confidentiality is protected. The LBMA has a Good Delivery List which is a de facto world standard for refined silver.

The LBMA is a trade association and should not be confused with an exchange however. It was established in 1997, it caters to a wholesale and not a retail market, it is particularly concentrated on over the counter, and it works to maintain and safeguard the efficiency of the London silver market. It upholds the quality of the product through the Good Delivery system and its polices probity amongst its membership. Naturally when I was putting this though compliance, which all good analysts must do at HSBC, I received a telephone call from our editorial department saying, "Jim, what's the meaning of probity", and I explained that it was the maintenance of high standards and perhaps she should apply this to the editorial department going forward, but nonetheless.

The functions of the LBMA include contact with regulators. There is little need for regulatory intervention because of the high level of professionalism in the market itself and the ability of the LBMA to police this. The LBMA provides statistics, documentation, and information. The London precious metals clearing, LPMCL, developed from a telephone clearing market to an electronic mechanism that provides allocated and unallocated accounts. Trading statistics are provided monthly by the clearing members, it's tabulated in values, quantities and the number of transfers. Note however that the clearing volume statistics in no way equate to the trading volume statistics. It's a common misconception, but it is only a fraction of actually what has been traded. Most producer and consumer contracts are transacted in London. London offers the vaulting facilities, which are really virtually unrivalled anywhere else.

London also plays an important role in the EfP or Exchange for Physical Market. Also the silver ETFs, the exchange traded funds, are held physically in London. This helps secure London's presence in the ETF market, and massive consumer markets help solidify London's position as the world's centre for silver markets. The central clearing mechanism and the vast pool of allocated and unallocated physical silver reduce the credit risk in the market. We have effectively massive pools of available bullion to offset liabilities. London also provides netting, which allows for greater efficiency and lower costs. The vaulting facilities are extensive and I think, in summation, London is, despite its detractors and despite the fact that repeatedly over history many other groups have said that they will wrest the silver market from London, London is likely to remain the focal point for world silver markets due to physical infrastructure, the delivery system, and the deep pool silver and available talent. That really is only effectively there in the city of London.

Thank you.