

Good as Gold

Interview with Paul Brady

Between 1999 and 2002, Gordon Brown ordered the sale of almost 400 tons of UK gold reserves when the price was at a 20-year low. Since then, the price has more than quadrupled, meaning the decision cost UK taxpayers an estimated £7 billion, according to accountants Grant Thornton.

Besides being a sign of the widespread lack of confidence in fiat currencies, the rising price of gold also demonstrates its continuing allure through the ages. We interviewed Paul Brady, Private Client Wealth Manager at The Henley Group, to introduce the current situation of the gold market.

In times of economic uncertainty, people always seem to trust more in gold than in currencies. Is that trust usually justified?

Absolutely. Currencies have a history of becoming devalued, and this tends to happen in 30-50 year cycles. Even the US dollar in the way that it currently operates, as a freely floating currency, has only been going for around 40 years. Before that it was pegged to the price of gold. And throughout history there are plenty of examples of inflation and hyperinflation to show how fragile currencies can be. But gold has stood the test of time as a store of value.

Gold has been used in currency at least as long as coinage, and the recent crisis again saw gold behaving more like a currency than a resource. What were the main factors behind that?

People are losing confidence in currencies to some degree. We're in uncharted waters after the measures that were taken in 2008, and it is probably only with hindsight that we will find out what the full effects will be. In any times of uncertainty and a loss of confidence, people look to assets that have historically done well. Gold has a history of surviving downturns and depressions.

Gold is only mined in a small number of countries in any great quantity. Have economic crises significantly benefited major producing countries like South Africa, China and Australia?

Yes it has benefited them, but not just through gold; countries with natural resources have benefited from price rises in all the main commodities in fact (Australia in particular). A great deal of China's recent growth has been driven by raw commodities. Chinese firms have also been 'forging partnerships' with many developing countries, particularly in Africa - all that means is that they are buying those countries' resources. In developing countries especially, I think there is a big question mark about how much of the population will really benefit from the recent rises in the cost of raw commodities. But governments and economies that hold gold reserves will undoubtedly benefit from these rises.

Gold extraction in China has risen appreciably in recent years, yet in South Africa it has fallen quite significantly. Is the slow rate of extraction likely to raise prices even further?

Certainly South Africa has been having major problems, especially with energy supply to its mines. All round, gold is becoming harder to extract there. China is now the world's largest producer of gold, but it is also its second largest importer.

As a natural consequence of supply and demand, when the supply of any asset decreases the value rises. Equally as a resource it becomes scarcer as people put a greater value on it; as with stamps, vintage wines, the work of certain artists, etc.

Nuclear physicists have in the past succeeded in the alchemists' dream of transforming lead into gold. Is there a risk that an advance in the technology for converting other elements into gold might reduce the overall value?

I would suggest not. Even if someone did develop a viable way of making lead into gold for example, it wouldn't be in their interests to develop large amounts of it. Not only that, it's also unlikely that they would be forthcoming about it.

But, if you know anyone who can do it, please do let me know! I'd be more than interested in having a chat with them.

The Indian Central Bank's recent acquisition of large quantities of gold has significantly driven up the price. Are we seeing a return to large-scale government gold-hoarding?

Yes. Over the past 10-15 years, governments have been net sellers of gold (though not to the extreme of the UK in 2001); now they are net buyers again. That's the first time that the acquisition mentality has come back. And it's not just India by any means; Sri Lanka and some Middle Eastern countries have been doing so openly, and we're almost certain that China and many others are quietly buying gold. Traditionally, most governments have kept their sales and acquisitions of gold secret.

The bulk of gold produced is made into jewellery (over 50%) and the second largest amount is kept as an investment. Do you think that that balance could change with the current inflation?

Yes, it will. Now the person on the street can invest in gold through ETFs (exchange traded funds) much more easily than he/she could ever have done before. That means people no longer have to physically buy gold (with its added costs of insurance etc.) in order to invest in it. That should swing the balance more towards the investment side, particularly if China fully opens up the gold investment market to its citizens.

But there's also a lot to be said for people wanting to hold the physical asset; gold jewellery has long been an important facet of Indian culture, and has also become very popular in China in recent years.

Everyone asks themselves this question, but what is your opinion: why do people place such a value on gold?

I think people set a value on gold, or any asset for that matter, based on perception. People will always speculate to try to make a profit; they like to have things that retain and go up in value. ■

