The Seven Ages of Gold

Central bank buying back to historical norm

David Marsh and Ben Robinson

Long-run changes in central banks' policies on buying and selling gold fall into seven distinct periods or ages over the past two centuries – the Seven Ages of Gold – each lasting an average of around 30 years.

The latest 'Rebuilding' Period VII has been underway since the financial crisis in 2008. In these eight years, central banks in both developed and developing countries have shown a new fondness for the yellow metal, rebuilding gold's importance as a bedrock of most countries' foreign reserves.

Following four decades after 1970 when central banks generally ran down their gold stocks, they have now returned to the historical norm of the previous 100 years of preferring accretions to disposals.

Annual net purchases of 350 tonnes a year over the past eight years have been in line with the 100-year average up to 1970 – reflecting the metal's renewed attractiveness as a safe haven asset in an environment of uncertainty and low or negative interest rates.

Developments since 2008 mark a powerful change from the 'Sales' Period VI in 1998-2008, when central banks, particularly in developed countries, were unloading bullion holdings. This is also in sharp contrast to the 'Demonetisation' Period V in 1973-98, when gold's role was in limbo after it was officially phased out of the monetary system in 1971-73.

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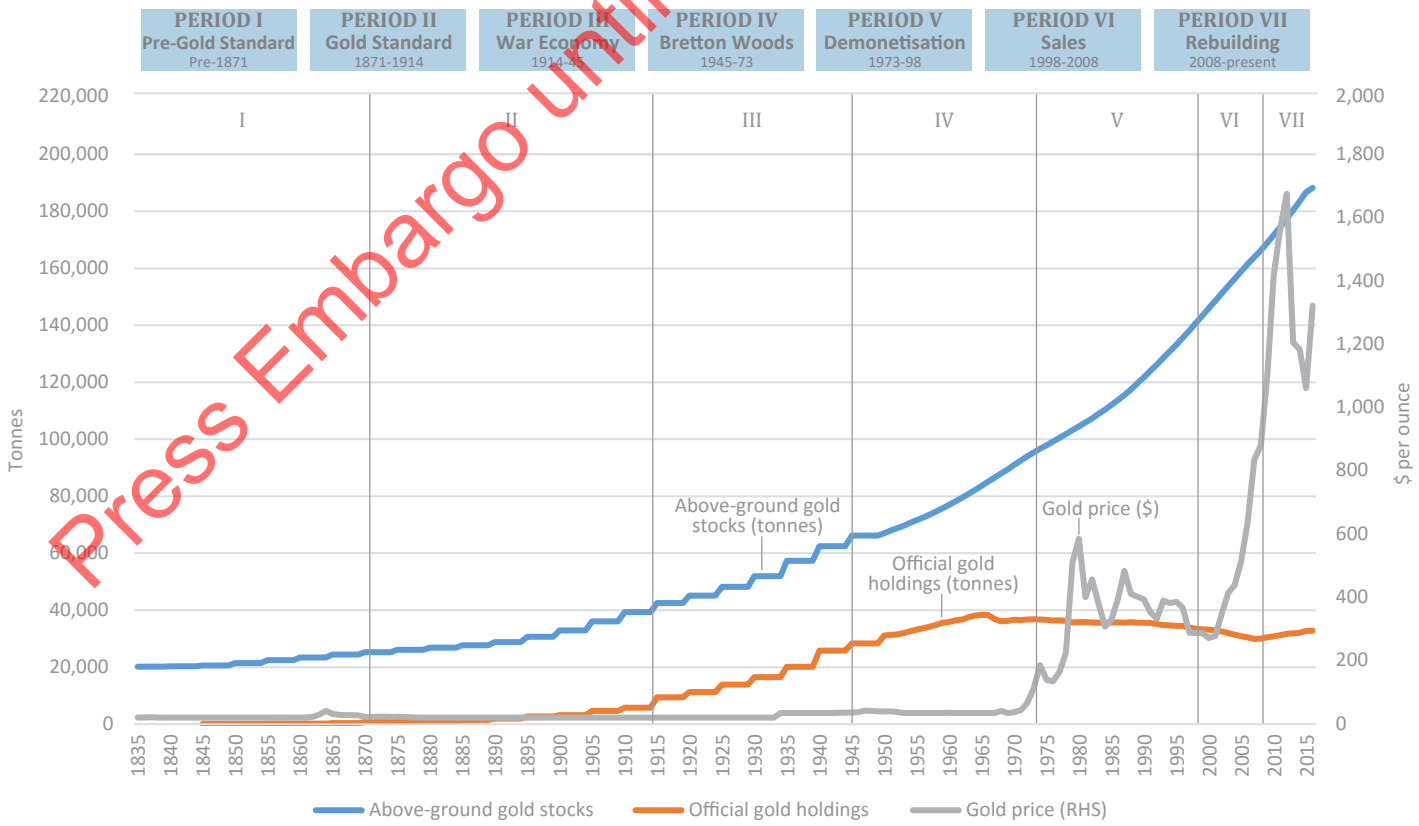
Central bank gold transactions have often been somewhat disassociated from the gold price. Central banks were net sellers over Periods V and VI, four decades of fluctuating but generally rising bullion prices.

In Period VII, central banks have been net buyers of gold every year since 2008, adding more than 2,800 tonnes or 9.4% to reserves. Developed countries (accounting for the lion's share of total official holdings) have been conserving stocks, and developing countries led by China and Russia have been building them up. This is the longest protracted spell of gold accruals since 1950-65, when central banks and treasuries acquired a net total of more than 7,000 tonnes during the economic recovery after the second world war.

The latest period since 2008 has been a time of sharp price swings in the $1,000 to $1,600 per ounce range. Central bank purchases appear to have been a factor behind the post-2015 price recovery. After the rises and falls of the post-war period, total gold holdings are back to the levels of the early 1950s. But there has been a shift over the past 70 years in gold distribution away from the US treasury towards European countries and, latterly, developing nations – symbolising the multipolar world economy.

The Seven Ages of Gold – how central banks' gold policies have fluctuated over two centuries

Above-ground gold stocks, tonnes, official gold holdings, tonnes, and gold price, $ per ounce, 1835-2015



Source: World Gold Council, GFMS, OMFIF estimates

KEY BULLION POLICY LANDMARKS FOR CENTRAL BANKS IN THE SEVEN AGES OF GOLD

The Seven Ages of Gold start with the 'Pre-Gold Standard' Period I before German unification in 1871. This triggered the widespread introduction of the system in which central banks' gold sales and purchases at a fixed price effectively regulated the world economy.

Broad international adoption of the gold standard ushered in Period II, from 1871. Central banks became the guardians of a fixed-price system, encompassing the build-up of Australian, South African and US mining output.

The 'Gold Standard' age ended in 1914, when the outbreak of the first world war caused suspension of the international gold system.

The 'War Economy' Period III runs from 1914 to 1945, spanning the reintroduction of the gold standard, the interwar depression, the gold standard's ultimate 1930s demise, and second world war dislocation that confirmed the monetary ascent of the US.

Period IV covers 1945-73, the Bretton Woods era of rising gold reserves, with European countries and Japan amassing sizeable new post-war holdings as central banks exchanged surplus dollars for gold from the US treasury.

Period V in 1973-98, after the severing of the dollar's official link to gold and the breakdown of the fixed exchange rate Bretton Woods system, was a time of falling official holdings and sharp gold price swings in response to world geopolitical tensions. Period VI in 1998-2008 was a time of gold sales by industrialised country central banks. As a result, even after the 2,800 tonnes of purchases over the past eight years of Period VII, total official holdings – at around 32,800 tonnes as of mid-2016 – are still more than 5,500 tonnes below the 1965 peak of around 38,300 tonnes.

An important milestone was leading European central banks' 2014 action in renewing an agreement, first signed in 1999, pledging a restrictive policy on gold sales for the five years to 2019.

One important reason why European central banks have preferred to maintain their gold stocks since 2008, switching away from the sales of the previous two decades, is because many banks inside the euro area regard their gold reserves as a hedge against potential monetary losses from imbalances and tensions affecting the single currency.

Based on long-term figures for gold holdings and world production, gold stocks in the hands of official institutions (central banks, treasuries and bodies such as the International Monetary Fund) appear to have steadied at around 17.4% of total above-ground stocks. This is down from 23% in 2000 and 40% in 1970, but marks stabilisation over the past decade following an earlier period in which central banks were net sellers.

The long-run figures, putting mid-2016 above-ground gold stocks at 188,214 tonnes, are based on data from the World Gold Council and the GFMS research group. Statistics on above-ground holdings need to make allowance for an unknown quantity of gold that is lost in industrial processes or otherwise unaccounted for in jewellery and investment usage. Reflecting the spread of modern mining technology and the entry of new countries into production, more than half of all the gold ever mined has been produced since 1970.

Gold's renaissance

One reason for gold's renaissance as a monetary asset has been developing countries' hesitancy about relying unduly on reserve holdings in dollars. China in particular seems to be following a strategy of using gold to counter the weight of the dollar.

Last year China lifted part of the veil over its gold reserves, breaking a six-year silence to reveal holdings of 1,658 tonnes as of June 2015 against the previously reported figure of 1,054 tonnes.

As of August 2016 it had 1,823 tonnes. Beijing moved to a market valuation of gold, which, according to latest figures, is worth $70.5bn, although this makes up only 2.3% of total Chinese international reserves.

China's total official gold holdings are judged to be sizeably larger. Metal from local mine production is believed to be held in a domestic account separate from the international gold holdings. The world's biggest official gold holder is the US, with 8,134 tonnes – more than four times that of China and more than five times Russia's 1,499 tonnes – followed by Germany with 3,378 tonnes, the IMF with 2,814 tonnes, Italy with 2,452 tonnes and France with 2,436 tonnes.

Showing the shift to a more diversified world monetary system, the US now accounts for just 25% of total official holdings, compared with 19% in 1900, 33% in 1920, 76% in 1940, 44% in 1960 and 23% in 1980. In future years, as economic clout moves away from advanced economies, developing nations are likely to build up further gold reserves as a proportion of total official holdings stocks. In the further development of the Ages of Gold, the metal's monetary renaissance that started in 2008 may have some way further to run. ■

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Fluctuations in US dominance: how major countries' gold holdings have shifted since the 19th century

Leading gold-owning nations: gold reserves as percentage of total world official holdings, 1880-2016

	National gold reserves as percentage of total official holdings										
	US	UK	Germany	Italy	France	Switzerland	Russia	China	Belgium	Netherlands	Austria
1880	18.2	14.8	7	1.9	21.1	1.2**	17.0	-	1.8	3	4
1900	19	6.2	6.6	3.6	17.1	0.9	20.8	-	1	0.9	10.1
1920	32.6	7.6	3.5	2.7	14.4	1.3	-	-	0.6	3.4	0
1940	75.7	5.7*	0.2*	0.5	6.9	1.7	-	-	2.5	2.1	0.2*
1960	44.1	6.9	7.4	5.5	4.1	5.4	-	-	2.9	3.9	0.7
1980	22.9	1.6	8.3	5.8	7.1	7.2	-	1.1	3	3.8	1.8
2000	24.5	1.6	10.4	7.4	9.1	7.5	1.2	1.2	0.8	2.7	1.2
2016	24.8	0.9	10.3	7.5	7.4	3.2	4.5	5.5	0.7	1.9	0.9

*Source: World Gold Council, GFMS, OMFIF estimates. *1940 uses 1935 national figures / 1940 totals. ** Uses 1885 data / 1880 totals*