Mining Journal

WGC turns its back on mining

The gold industry is offering investors a horse and buggy in an age of autonomous electric cars forcing even its principal lobbyist to change direction.

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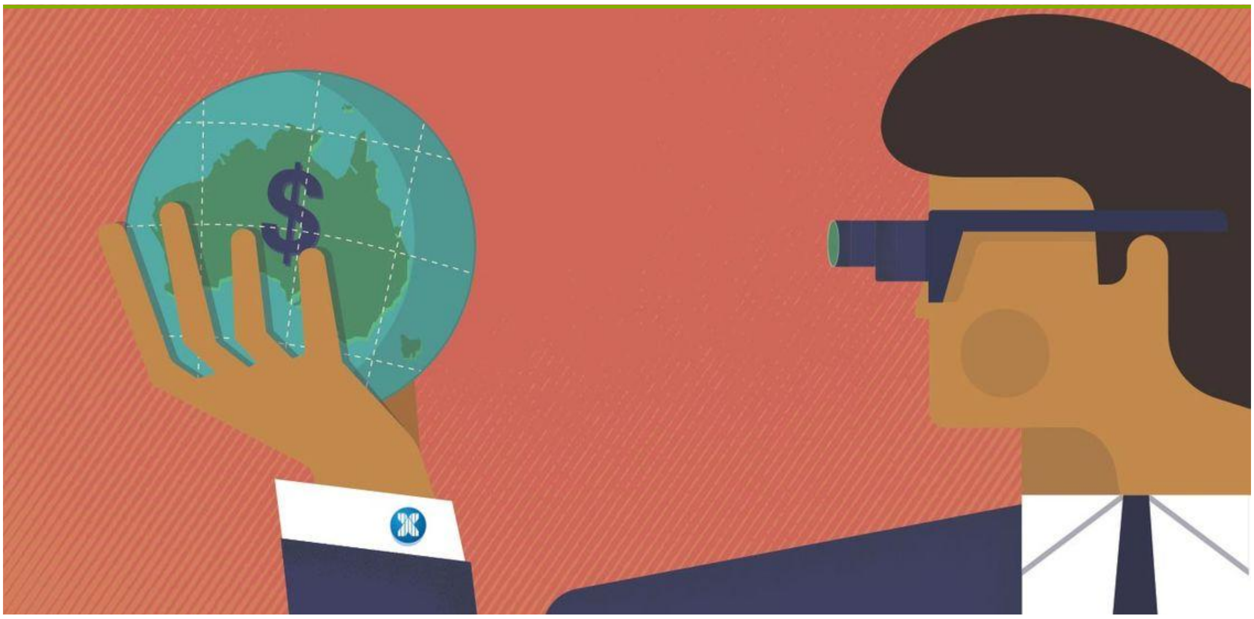

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To commemorate its 30th anniversary, the World Gold Council (WGC) recently published a compendium of views of what the gold market could look like 30 years from now.

In his foreword to ‘Gold 2048: The next 30 years for gold', chief executive Aram Shishmanian conceded that his WGC could not pretend to have all the answers but, he reassured his readers, "we have certainly tried to ask the right questions".

Unsurprisingly, the selected contributors to the volume generally portrayed the future positively. Even the chapter documenting the reasons for a long-term decline in global mine output ended on a rosy note.

Discovery of Witwatersrand-style mineralisation in the Pilbara "could be a step change", according to the hopeful author of the section on the mining outlook, and "help to dictate the course of gold production over the next three or so decades".

Despite his claim to have asked the right questions, Shishmanian's team ducked the most obvious question for an organisation established by miners to boost their profits: Is the gold price higher than it would have been without the group's lobbying efforts? Or, put another way, if the WGC closed immediately, would the gold price fall?

Gold is a well-established investment medium with unmatched grassroots support extending from individuals to governments and institutions wherever pools of wealth exist. Relative movements in financial asset prices and changes in the pool of global wealth are likely to remain the primary drivers of the gold price. The WGC's own analytical output points to as much.

The role of the WGC has changed dramatically since it was established in 1987, amidst two decades of disappointingly poor gold-price returns, with a mandate to expand industrial use. Today's WGC has morphed into a deceptively camouflaged financial services company relying increasingly on turnover and less on price.

> **With the advent of the next generation of financial product technologies existing assets will necessarily command a smaller share of global wealth**

Reuters quoted an unnamed source in early May saying that the WGC would supplement its exchange-traded gold fund established in 2004 (GLD) with a new, cheaper ETF "to fend off rivals with lower charges".

The WGC had previously shored up its funds management presence in 2017 with a more expensive and technically sophisticated fund (GLDW) holding long positions in gold with short positions in a basket of foreign currencies.

The latest filings available from Companies House in the UK show that 62% of total WGC spending of $116 million in 2016 related to sponsorship of its GLD exchange-traded gold fund. Overheads were another $31 million. Only $13 million was spent on non-ETF gold marketing activities in a business sporting a net profit of $29 million and cash and gold assets of $101 million.

Consistent with the WGC effectively dumping the interests of the mining industry in favour of funds management, membership fees that had exceeded $28 million in 2013 have been abandoned.

The organisation's financial viability now depends on investors maintaining enthusiasm for structured gold investments that compete directly with the equities of gold mining companies. The offspring is devouring its parents. There is no mention of this diversion of interests in the WGC celebratory report.

Another matter going largely unaddressed in the group's preview of the future is the role of technology in fostering a rapid proliferation of stores of value and transaction media.

The WGC defiantly rejected suggestions crypto currencies could threaten the role of gold, in a January 2018 investment update.

All the reasons presented for gold's superiority over crypto currencies, including its role as a hedge against inflation, its much lower volatility and being uncorrelated with other assets, rest on an extremely short crypto currency trading history.

It would be just as silly to base judgements about gold's investment usefulness entirely on how its price fared immediately after being freed from its link with the US dollar in 1971.

Whether investors decide crypto currencies can add to portfolio outcomes either without or in conjunction with gold will be data driven and currently unknowable, albeit subject to speculation. Also unresolved for the moment is the nature of future regulatory and custody regimes that will impact whether crypto currencies get a position in the investment mainstream.

In any event, crypto currencies have an outstanding competitive advantage over gold: wherever internet access exists, some can be used as money in even the smallest transactions.

As my high school economics text memorably elucidated with the example of cigarettes in prisoner of war camps, money is whatever people are prepared to accept to facilitate trade in goods and services.

The WGC may be too tied to its once innovative but now commonplace investment structures, buffeted by competitive forces, to offer an objective view of how gold will be used in the future or what might take its place.

For at least 30 years, financial markets have been driven by technology. From the Black Scholes option pricing model to credit default swaps, products have been engineered in anticipation of a use being found.

Today, gold moves seamlessly from mine to refinery to vault. If investors could be assured of the gold content of mineral resources, there may be no need to dig it out from its naturally occurring underground vaults. Capital could be dedicated to continually improving the quality of resource estimates.

Might the blockchain technology actually offer a new medium for pricing and allocating gold resources without the need to waste billions of dollars on unnecessary mining? This is another unaddressed question.

With the advent of the next generation of financial product technologies - because there is no reason to expect financial innovation to suddenly cease - existing assets will necessarily command a smaller share of global wealth or transactions.

Gold will still play a role in financial markets just like plywood futures or any number of other products but its ranking, along with those of other financial assets, is at risk.

Only a catastrophic failure of the underpinning new technologies might force investors to revert nostalgically to how things used to be.

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