Macroeconomic Trends That Are Influencing The Yellow Metal

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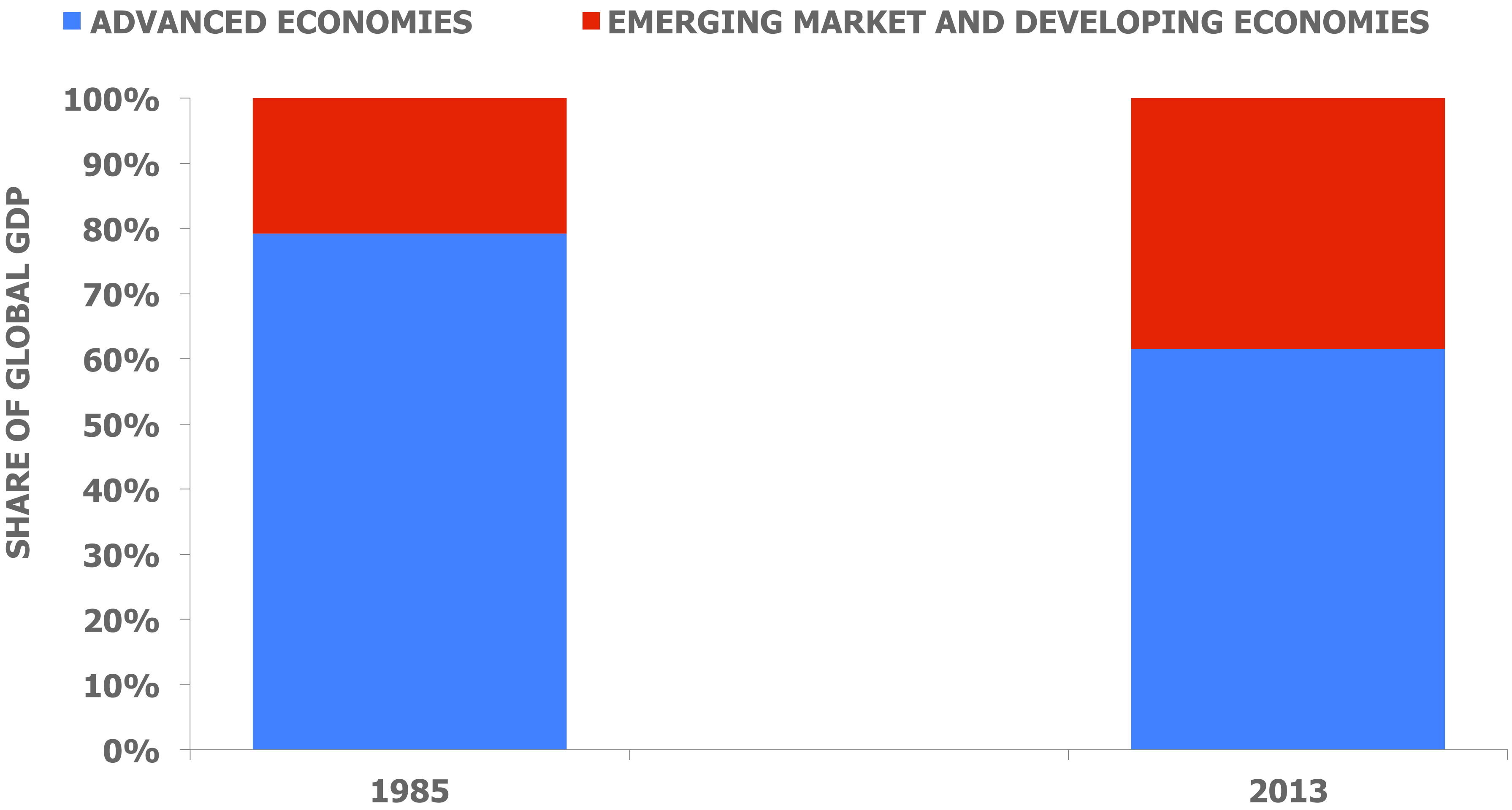
KEY MACROECONOMIC TRENDS?

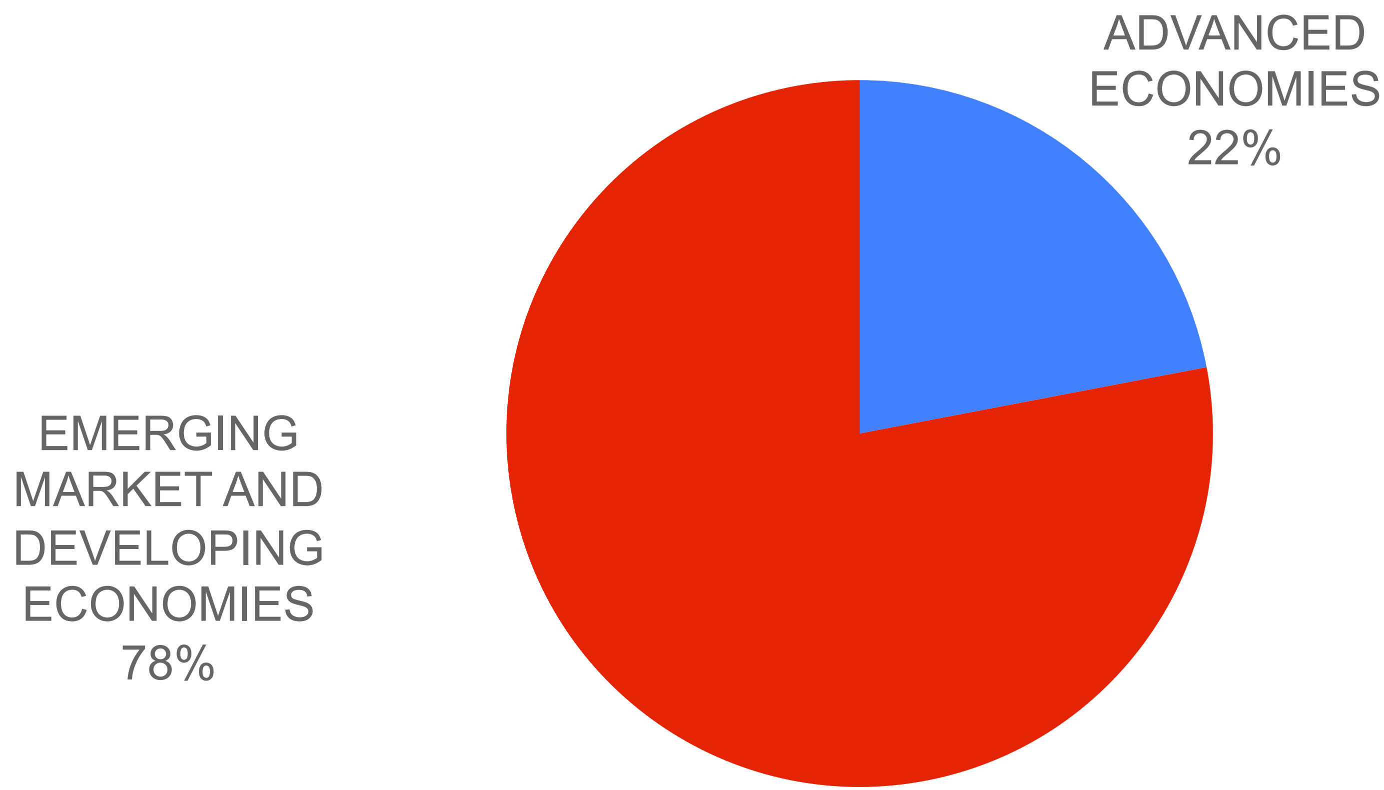
- Need to focus on those economic trends that are especially relevant to the gold market and, most importantly, to determining gold prices:
  - Changing shares of global GDP, with Emerging Market and Developing Economies' growing importance compared to Advanced Economies.
  - Rise in debt, particularly in the developed world but also in China.
  - Growing long-term fiscal problems in USA, Europe and Japan.
  - Monetary policy response to economic crisis and its consequences.

SHARE OF WORLD GDP IN 1985 AND 2013



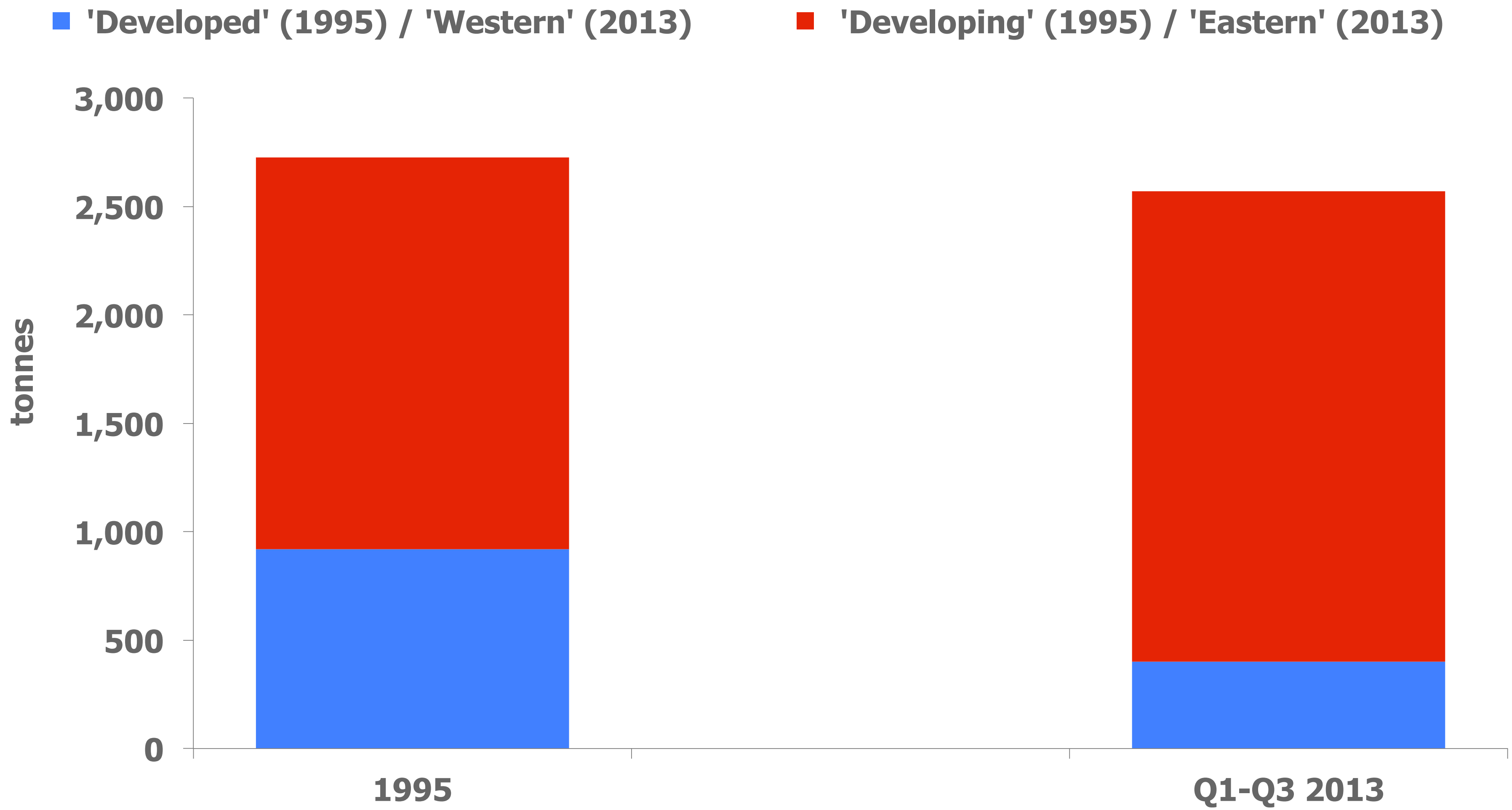
Source: IMF

CONTRIBUTION TO WORLD GDP GROWTH 2009-13



Source: IMF

SHARE OF GOLD JEWELLERY AND PHYSICAL BULLION* DEMAND IN 1995 AND Q1-Q3 2013

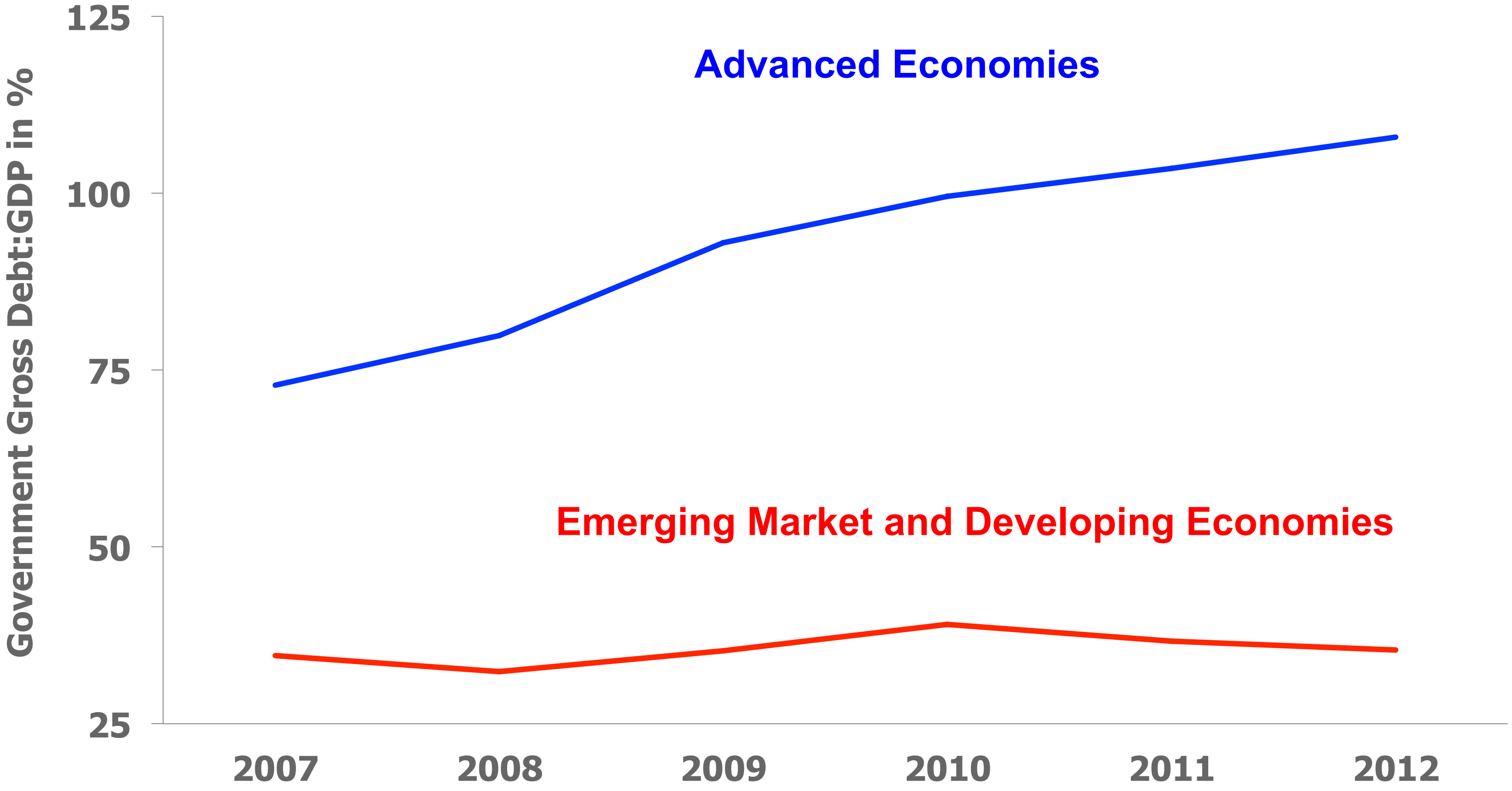


Source: World Gold Council (*physical bullion demand refers to direct physical purchases of bars and coins)

IMPACT OF CHANGING SHARES OF GLOBAL GDP AND GOLD DEMAND

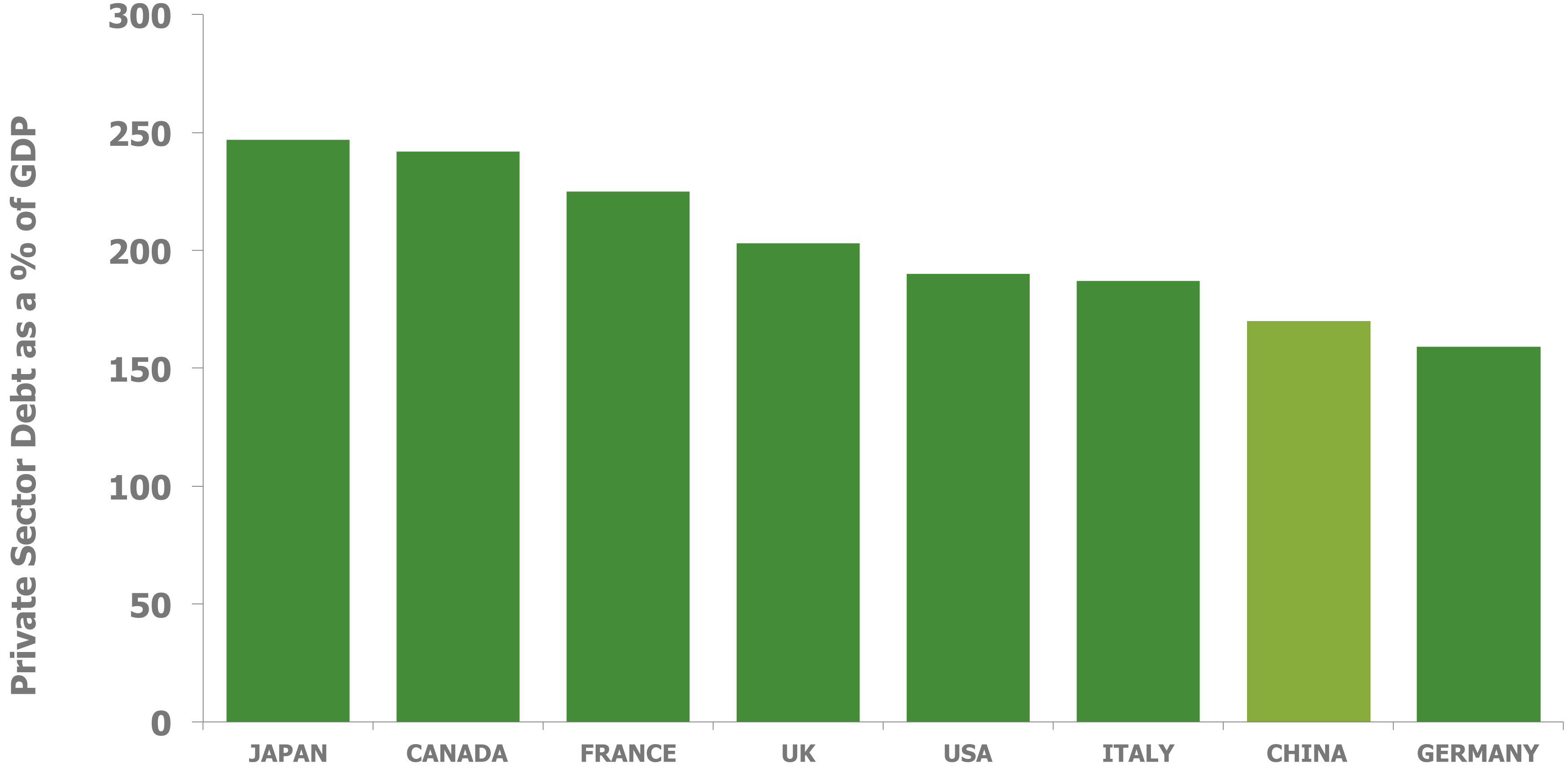
- Jewellery ever more focused on Emerging Markets and Asia in particular
- Physical bullion market has also shifted 'East', with a noteworthy and growing contribution from China (e.g. latter's huge rise in bullion imports).
- Although such 'Asian demand' tends to be "reactive" and a "price taker" its impact on gold price formation and activity is growing.
- Moreover, Emerging Markets (especially China) have a growing impact on the 'paper markets' for gold both through trading on domestic exchanges (e.g. SGE, SHFE) and also indirectly via the loco-London market.
- Their growing share of global GDP coupled with financial liberalisation and, in many cases, a traditional affinity for the 'yellow metal' should in future see Emerging Markets led by China become still more important in terms of gold demand and price determination.

GOVERNMENT DEBT LEVELS HAVE RISEN SHARPLY IN THE ADVANCED ECONOMIES



Source: IMF

PRIVATE SECTOR DEBT LEVEL VERY HIGH IN MOST G7 ECONOMIES AND RISING FAST IN CHINA



Source: OECD

IMPACT OF HIGH PRIVATE AND PUBLIC SECTOR DEBT LEVELS ON THE GOLD MARKET?

- In wake of the 'credit bubble' bursting, the Advanced Economies are experiencing the deflationary impact of austerity and much slower credit growth as both government and private sector forced to de-leverage. This is restraining consumption, with a negative impact on jewellery demand.

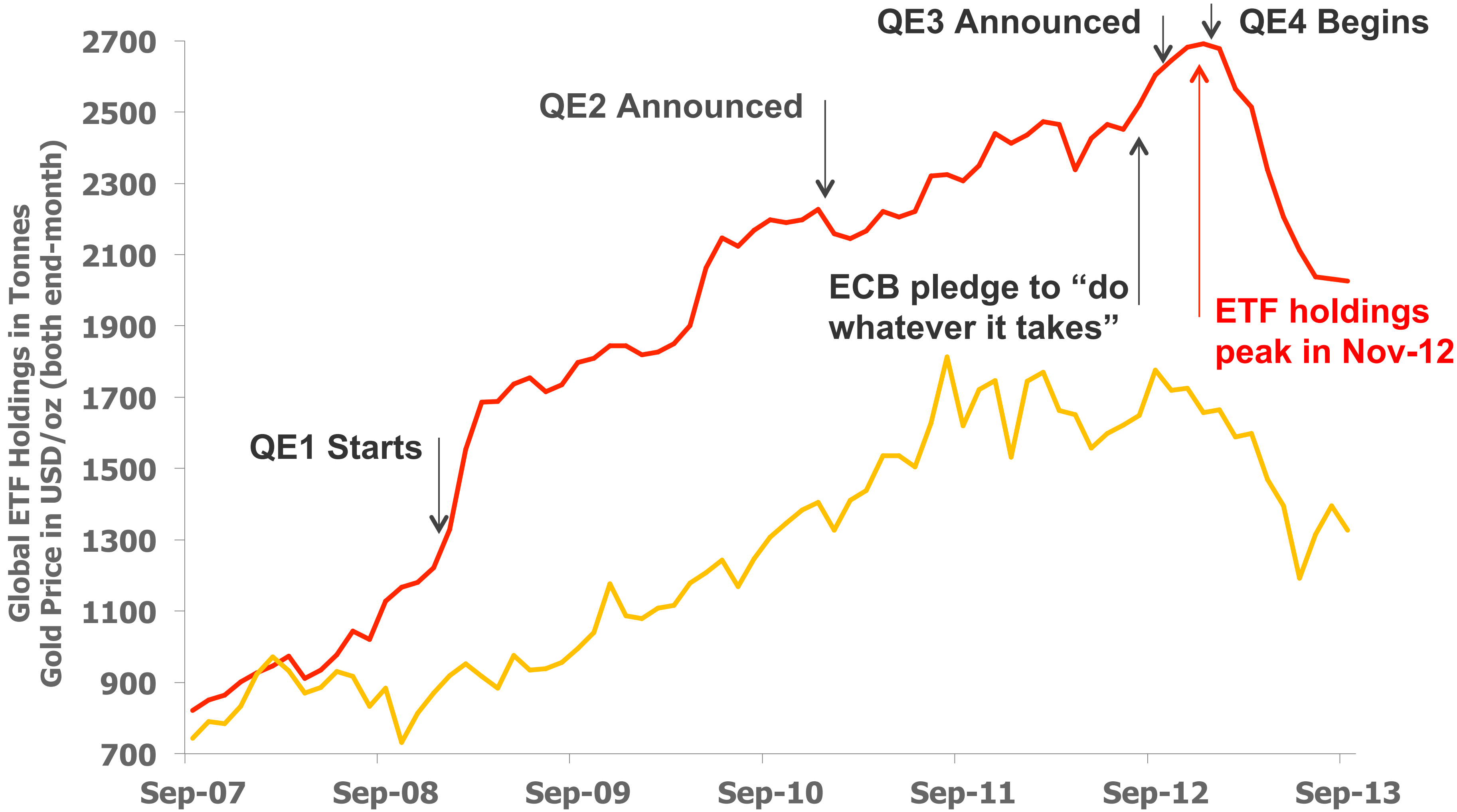
- Also, weak GDP and credit growth means that inflation is kept at a low level, which reduces the appeal of gold to investors. 'Distress sales' of old jewellery have contributed to push up the amount of gold recycled.

- Massive expansion in credit in China since 2008 has helped to maintain a high rate of GDP growth and personal consumption. This has boosted both jewellery and investment demand for gold in recent years.

- High debt levels in USA and Eurozone have undermined credit quality of government debt and by extension trust in the USD and EUR, encouraging some Emerging Market central banks to seek portfolio diversification through gold purchases.

- Political and economic costs of de-leveraging and austerity coupled with already high tax burdens in many 'Western' countries are undermining the commitment to anti-inflation policies. In most Advanced Economies the view that higher inflation would be beneficial has gained ground amongst policy makers, economic commentators and the general public. This is likely to be very "gold-positive" in the longer run.

MONETARY POLICY A KEY FACTOR IN DETERMINING GOLD INVESTMENT AND PRICE LEVELS



Source: Thomson Reuters GFMS, LBMA

MONETARY POLICY RESPONSE TO THE CRISIS HAS HAD A VARIABLE IMPACT ON GOLD PRICES

- Ultra-low interest rates and Quantitative Easing (QE) in the USA helped drive the ‘Western’ investment led gold bull market from 2009-11. But positive impact of QE2 on investment and the gold price began to wane in 2012.

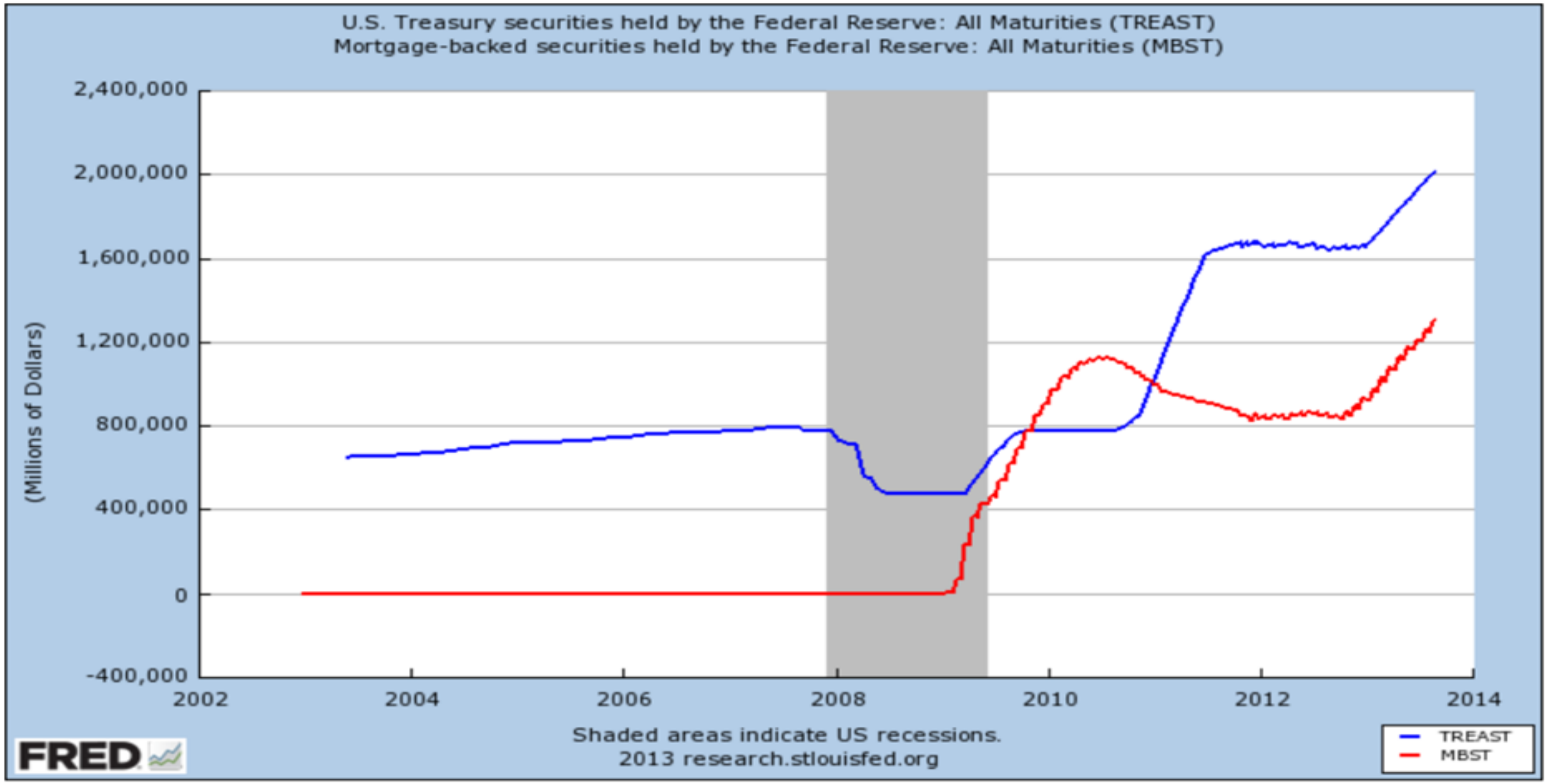
- Expectations of QE3 boosted investment and gold prices during summer of 2012. But, subsequent to this new policy being announced in September 2012 and, still more so, QE4 in December 2012, such measures have arguably had a ‘negative’ impact on gold. It would seem that this has been related to the stock market rally QE3 and QE4 have to a large extent produced: S&P 500 climbed by 26% between 12/09/12 and 29/11/13. A shift out of gold and into equities has been an important trend since Q4 2012.

- In Europe, the ECB’s pledge “to do whatever it takes” to defend Euro and associated aggressive monetary policies to support the single currency and Eurozone banks removed a major support for gold from those investors in the yellow metal that had feared a banking crisis and a collapse of the Euro.

- Even prior to Bernanke’s comments in June 2013 on possible Fed “tapering” investors had begun to more seriously consider the possibility of tighter monetary policy in the USA in 2014, which resulted in reduced investor interest in gold that played an important part in the major drop in gold prices during the first half of 2013.

MASSIVE INCREASE IN US CENTRAL BANK'S BALANCE SHEET POST-LEHMAN FAILURE

U.S. Federal Reserve: Treasury and Mortgage-Backed Securities Held



INFLATION RISKS OF PAST "QE" POLICIES MAY STILL BE POSITIVE FOR GOLD IN FUTURE

"Inflation is always and everywhere a monetary phenomenon in the sense that it is and can be produced only by a more rapid increase in the quantity of money than in output."

Milton Friedman

- Currently deflation still a far greater near term risk than inflation, a fact that helps to explain the weakness of gold prices.
- Inflation fears prompted by beginning of QE policies and massive expansion of central bank balance sheets have so far turned out to be misplaced.
- But, if economic activity in the USA, Japan and Europe picks up strongly and central banks are "behind the curve" in tightening monetary policy then the currently 'latent' increase in money supply may become activated, which together with a higher velocity of money in circulation would lead to much greater rates of inflation.
- This could well result in a renewed investor-driven gold bull market in the medium term future.

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