

# Crucible



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By Singapore Bullion Market Association

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# EDITORIAL

This bumper issue of Crucible was planned in conjunction with the 4th Asia Pacific Precious Metals Conference, originally scheduled for June 2020. But as dark clouds gathered earlier this year in the early stages of the pandemic, we made the difficult decision to cancel the event, and to instead focus our efforts on maintaining our services to our members and developing digital outreach strategies during this period of disruption.

We have maintained close communication with our network, and among other activities, have worked with the World Gold Council on a market survey among our members on development strategies for Singapore's gold bullion market, and organised webinars with Singapore Exchange (SGX) as part of its Commodities Unplugged series. The panels, which focused on challenges to the supply chain amid Covid-19 and price drivers and outlook for the global precious metals markets, saw encouraging response by speakers and participants alike.

The stability of gold during the pandemic has vaulted the precious metal into the clear view of investors and markets, and only highlights its importance as part of investor portfolios in an unsure economic future. While gold mining and recycling/refining activities were curtailed due to the lockdown, the gold market's supply chain has also shown remarkable resilience amid the disruption.

The previous issue of Crucible 13 published in March focused on the impact of Covid-19 on the sector, and provided an update to members and subscribers with an interest in this part of the world. This bumper issue, Crucible 14, is again a showcase of our connectivity, even during the pandemic, bringing together valuable insights from markets like Australia, Indonesia, Japan, Russia and South Korea, which are not often covered in the media.

The coronavirus shock is unprecedented and even sharper than the global economic crisis in 2008, but I believe a decisive policy response by governments worldwide, if delivered in a successful and timely fashion, can prevent lasting damage to the global economy. The rate of Covid-19's growth looks to be slowing in many regions and stringent shutdown measures are gradually being lifted, including in Singapore, which has just emerged from its partial lockdown and is gradually reopening its economy in stages.

I hope we can build on the interest and momentum going forward, and I look forward to meeting with you again as we return to normality.

## Albert Cheng

CEO, Singapore Bullion Market Association

# SBMA News

BY ALBERT CHENG, CEO, Singapore Bullion Market Association

Here's an update of our activities:

**APRIL 14, 2020:** CEO Albert Cheng was featured by Japan Bullion Market Association on its YouTube channel, where he spoke about about the measures undertaken by the Singapore Government for Covid-19, and how the pandemic has disrupted the gold business in ASEAN countries.

**JUNE 2, 2020:** SBMA participated in the webinar "New Opportunities between ASEAN and China Gold Markets in the Post Covid-19", organised by Shanghai Gold Exchange International. SBMA members Chow Tai Fook, MTS Gold, UOB, and YLG Group also participated.

**JUNE 4-5, 2020:** SGX Commodities Unplugged – webinar series on precious metals organised by SBMA and managed by Foretell Business Solutions.

Day 1 | 2020 Asia Pacific Precious Metals Markets — Challenges to The Supply-Chain Amid COVID-19

Day 2 | Global Precious Metals Markets — Price Drivers and Outlook

To receive a copy of the presentation or synopsis of the sessions, kindly write to [info@sbma.org.sg](mailto:info@sbma.org.sg)

## UPCOMING EVENTS

6-8 June, 2021. Singapore

### Asia Pacific Precious Metals Conference 2021

APPMC, organised by the SBMA and supported by Enterprise Singapore, returns for its fourth edition. More information, updates and details of past conferences are available at: <http://www.asiapacificpmc.com>

## About Crucible

Crucible is published quarterly by SBMA. If you would like to contribute an article, news or information to Crucible, place an advertisement in Crucible, or if you require further information, please contact:

Singapore Bullion Market Association,  
9 Raffles Place, Level 58, Republic Plaza,  
Singapore 048619, Singapore.  
Tel: +65 6823 1301 / +65 6823 1302  
Email: [mail@sbma.org.sg](mailto:mail@sbma.org.sg)  
Web: [www.sbma.org.sg](http://www.sbma.org.sg)

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# THE EFFECTS OF COVID-19 ON AUSTRALIA'S PRECIOUS METALS MARKET

BY BRON SUCHECKI, *Senior Precious Metals Project Analyst, Pallion*

*Evolution Mining's Mount Rawdon Gold Mine, Queensland, Australia*

As the world's number two gold producer (and forecast to overtake China in 2021),<sup>1</sup> Australia has been crucial in supporting global precious metals markets as Covid-19 has upended the industry's established financial and logistics networks.

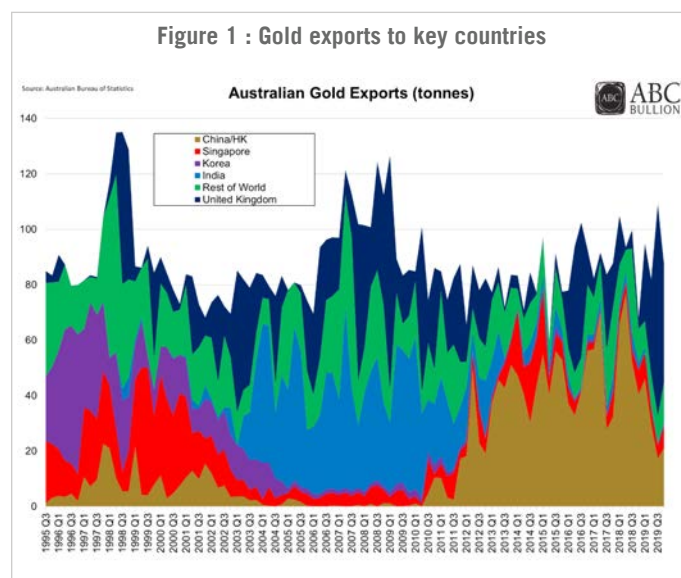
## AUSTRALIA'S PRECIOUS METALS MARKET

Australia produced 326 tonnes of gold in 2019, and its output is forecast to rise to 383 tonnes by 2021. In addition, Australia also imports around 100 tonnes of doré and scrap from neighbouring countries such as Papua New Guinea, Thailand, Japan and New Zealand.

The Australasian refining market is serviced by two London Bullion Market Association (LBMA) and Shanghai Gold Exchange-accredited refiners, with ABC Refinery holding a 43% market share of gold and silver doré total combined throughput of 12.6 Moz and Perth Mint with the remaining 16.7 Moz.<sup>2</sup>

With a population of only 25 million, almost all of the approximately 450 tonnes of gold refined in Australia is exported. While there is a healthy domestic precious metal market anchored by the two internationally recognised refining brands and serviced by a group of around 25 smaller bullion retailers, Australia's stable political history, geographical isolation and solid economy works against more widespread appreciation of gold's benefits compared to countries like Germany or the United States (US), which have a much higher awareness of precious metals among their populations.

Given Australia's geographical proximity to India and China, most of its gold output has historically flowed to those countries (fig.1).



Source: Australian Bureau of Statistics

An interesting feature of the data is the shift from Singapore and Korea towards India from 2003 to 2011. Increasing hostility by the Indian government towards gold, via increased duties and other measures, as well as more aggressive sourcing by Indian refineries of gold direct from miners, has resulted in the decline of India as an export destination and for China to emerge as the major consumer.

As a major gold trading location, any faltering in Asian demand (as has occurred recently) results in an increase in shipments to the United Kingdom (UK) and future export figures will show both the UK and US as destinations for Australia's gold output.

### IMPACT OF COVID-19

The disruption caused by Covid-19 to gold's supply chain has been significant, resulting in:

- A reduction in mine output
- Closure of key refineries in Switzerland
- Transport/logistics impacts
- Reduction in trading desk risk appetite

The divergence in the gold price between New York and London is the most visible manifestation of the friction the coronavirus has created in the gold market's financial and logistics networks.

With Australia having taken decisive action in response to Covid-19, Australian producers and refineries have been open for business. ABC Refinery has experienced more enquiries for refining work by those looking to take advantage of our per annum capacity of over 400 tonnes of gold and 750 tonnes of silver to substitute for closures elsewhere.

ABC Refinery has also experienced increased sales from firms able to take advantage of the large New York-London exchange for physical as well as having the ability to consume and value add metal through its mine-to-market approach via the ABC Bullion range of bullion products and trading facilities, as well as jewellery, industrial products and vaulting services in associated group companies.

Freight and logistics were classified as essential services in Australia and domestic producers have continued to operate with minimal interruption due to:

- Implementation of longer rosters to help limit the number of people on site and allow separation of workforce for business continuity.
- Producers strategically positioned near regional workforces not affected by limitations on fly-in fly-out (FIFO) workforces.

ABC Refinery has implemented strict business continuity measures to ensure operations are not impacted. While freight and logistics have been impacted, ABC Refinery's strategic location in Sydney (a major freight forwarding hub) means we have not encountered any roadblocks to date in supplying bullion to the Asian market as well as London and New York. We have also been working on innovative solutions by offering delivery loco-Sydney or even storage solutions at our independent vaulting service Custodian Vaults.

In addition, ABC Refinery has recently opened a trading office in Perth to service the growing demand for its refining and trading services in Western Australia. Former deputy CEO Joe Metcalfe, deputy treasurer Nishan Kodituwakku and senior trader Michael Dymock from the Perth Mint have been a welcome addition to our team.

### OUTLOOK

Equity and bond markets have shown huge volatility and investors have lost a lot of value in equities worldwide. The addition of some wild and very painful swings in bond markets, just when bonds would normally be expected to protect investors from weakness in equities, has focused investors on gold's safe haven attributes.

## THE DIVERGENCE IN THE GOLD PRICE BETWEEN NEW YORK AND LONDON IS THE MOST VISIBLE MANIFESTATION OF THE FRICTION THE CORONAVIRUS HAS CREATED IN THE GOLD MARKET'S FINANCIAL AND LOGISTICS NETWORKS.

Investors are worried about indebtedness on two fronts:

- Corporate leverage will amplify the pain felt by those companies most exposed to the economic impact of the coronavirus; and
- Deterioration in government finances as they respond to the coronavirus.

The supply of government debt coming to the market will likely have to be dramatically increased, weakening the bond market, and unconventional monetary policies will continue to drive down interest rates for longer, making gold a natural choice for investors both large and small.

As countries contain Covid-19 and lockdown restrictions ease, ABC Bullion feels that the outlook for gold remains strong based on two key demand drivers:

1. *The rise of middle market demand.* There have always been two keen followers of gold: the retail side of the market and commodity trading advisors who come in and out of the market. Covid-19 will result in growing awareness of the role of gold in the great "middle", who have either bypassed the gold market, or whose advisors have bypassed gold on their behalf.
2. *Official and government demand.* There has been a trend for central banks in the east to accumulate gold and this will be spurred on by the stresses caused by Covid-19. The US was all for a trade war with China in the months before the coronavirus appearing, and the official sector will be additionally cautious about the diversification of their portfolio in a post-Covid-19 world.

Given the above, ABC Bullion is bullish on gold demand and therefore price. Before Covid-19, gold had experienced increasing institutional interest and a return of retail investors. The coronavirus will accelerate that interest as it underscores the diversification benefits that gold provides to investor portfolios.

### Notes

- 1 Australian Government Department of Industry, Science, Energy and Resources - Resources and Energy Quarterly, March 2020. <https://www.industry.gov.au/data-and-publications/resources-and-energy-quarterly-march-2020>
- 2 Refinitiv - ABC Refinery: A new emerging force in the Australian precious metal refining landscape, 26 November 2019. <https://www.linkedin.com/pulse/abc-refinery-new-emerging-force-australian-precious-metal-alexander/>



**BRON SUCHECKI** is Senior Precious Metals Project Analyst at Pallion, covering precious metals research for ABC Bullion and internal projects within the wider Pallion group. Bron has over 25 years' experience in the precious metals industry across retail, treasury, depository, and risk areas.



# WILL COVID-19 SLOW GOLD PRODUCTION IN RUSSIA?

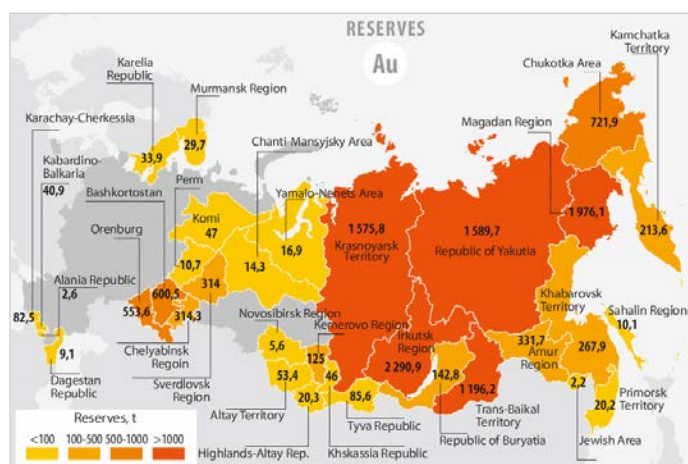
BY SERGEY KASHUBA, *Chairman, Union of Gold Producers of Russia*

*A mine operated by Polyus, the largest gold-mining company in Russia and the world's fourth largest.*

The Russian Federation has about 14,600 tonnes of gold in reserves in situ, according to the Russian Classification of Reserves, which places the country among the top three nations globally in terms of gold reserves in the ground. The average grade of gold reserves in Russia is slightly above the average grade of the majority of other gold mining countries. Gold is mined in 25 regions, notably in Siberia and the Far East.

## GOLD RESERVES IN RUSSIA

Gold production in Russia has been steadily growing over the last 30 years, making the country among the three leading gold producing countries in the world. In 1991, Russia mined 168 tonnes of gold, a figure that has grown to 330 tonnes in 2019.



Source: RosGeoFund FBGU

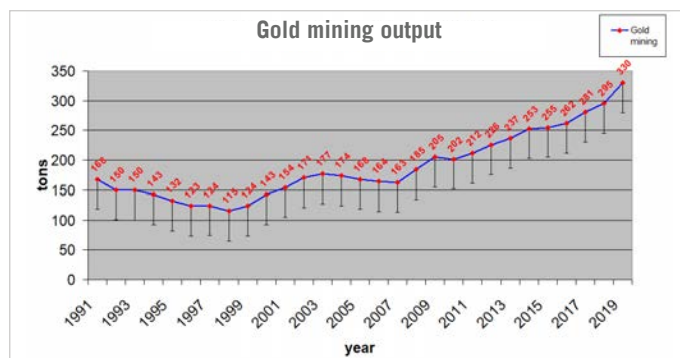
The top five companies produce 50% of the gold in Russia; the 25 largest companies account for 80% of overall production, while the remaining 550 companies produce about 20% of the overall gold production in Russia. As a result of the prevailing high gold price and heavy investment made by gold mining companies, gold production in Russia grew by an average of 3% to 6% per year from 2010 to 2019.

## RECORD PRODUCTION

According to the Union of Gold Producers of Russia, a non-profit organisation whose members produce over 70% of gold in Russia, gold production in Russia reached a record in 2019, in particular:

- Production from hard-rock and alluvial gold deposits grew by 10%, amounting to 287 tonnes;
- By-product mining from complex polymetallic deposits grew by 17.5%, amounting to 18 tonnes; and
- Production of gold in concentrates from refractory ore grew by 46%, amounting to 25 tonnes.

While noting a surge of 10% of gold production from hard-rock and alluvial deposits in Russia in 2019 compared to the preceding year (in absolute numbers, it amounted to 25 tonnes), it is worthwhile mentioning the companies that contributed to the overall increase in gold production: Polyus, Polymetal, Petropavlovsk, Nordgold, Kinross Gold, Highland Gold Mining, Bystrinsky GOK (Norilsk Nickel), and Susumanzoloto.



Source: Ministry of Finance of Russia, company reports



Since 2012, **SERGEY KASHUBA** has been the chairman of the Union of Gold Producers of Russia (UGPR), an association of gold mining companies in Russia that together produces about 70% of the country's gold. His experience in the industry spans 15 years in various mining companies, where he specialised in evaluating gold deposits in Russia and CIS countries and in structuring

M&A deals of gold deposits. From 1999 to 2002, he chaired the Russian Banking Association's precious metals committee. Previously, he was the chief of the precious metals department at various Russian banks. He graduated from the Institute of Foreign Languages and worked in various state organizations before moving into the private sector.

Following the outbreak of the coronavirus earlier this year, approximately one-third of the world's biggest gold producers revised their forecasts for gold production in 2020. The Union of Gold Producers of Russia, which updates its forecast for gold production in Russia annually, believes the impact of the coronavirus on gold production in Russia is minimal at the moment, and that the pandemic will not result in a substantial drop in gold production. We remain firm in our belief that Russia will maintain its strong gold mining output from the previous year.



# CONSUMER BEHAVIOUR TOWARDS GOLD JEWELLERY IN INDONESIA

BY JENNIFER HERYANTO, *Chief Executive Officer, SKK Jewels*

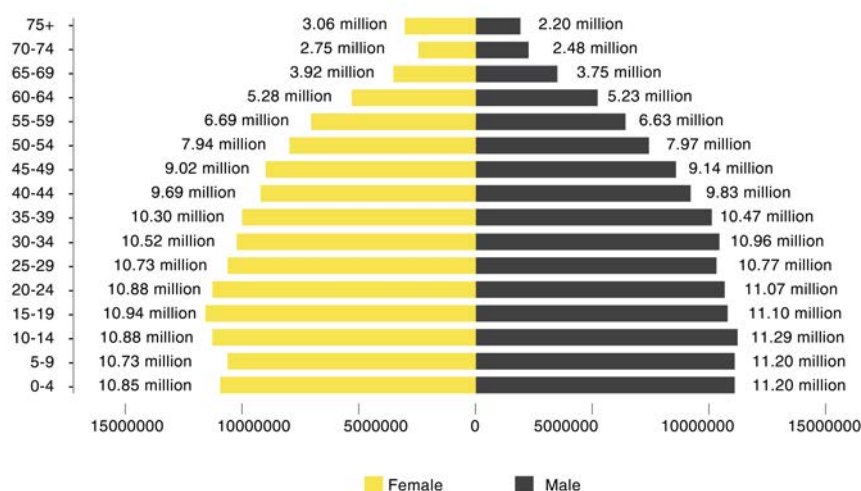
As the world's fourth most populous country, Indonesia has become the focus of many global firms and industries. With more than 270 million inhabitants spread out across 34 provinces on seven big islands, the country is considered Southeast Asia's economic engine. Although it has favourable prospects for sustainable businesses and is forecast to be among the world's four largest economies by 2030 (Economist Intelligence Unit), the country is still considered a blank canvas for many global firms, including gold industry players, due to its unclear regulation, sophisticated demographic segmentation, and lack of information of the industry landscape.

## DEMOGRAPHIC DIVIDEND

A large share of Indonesia's population will be of working age in the coming decades – what is known as the demographic dividend or the demographic bonus – giving it a competitive advantage compared to more developed countries facing an ageing population. The size of the country's economically active population – aged between 16 and 65 – is growing and expected to peak at 70% of the total by 2030. The median age of Indonesia's population is currently 29.7 years old – an attractive proposition for any business (fig.1).

Gold jewellery's main consumer demographic – females from 20 to 54 years old – comprises around 26% of the population, or 69 million people, which is more than Italy's total population and almost 12 times of Singapore's total population. The income of this population is also growing along with the share of employment of the total female population (from 45% in 2011 to 50% in 2019, according to the Indonesia Statistics Bureau). Additionally, the minimum salary

Figure 1 : Indonesia's population by age (2020)



Source: Indonesia's National Statistics Bureau, 2019

has also increased significantly in the past 10 years. For example, in Jakarta province, it has grown almost fourfold from IDR 1.11 million (US\$79) per month in 2010 to IDR 4.27 million in 2020.

The country has another competitive advantage: its growing middle class, fuelled by rising incomes. In general, Indonesia's population is divided into three segments: upper class, middle class, and lower class, with the majority falling into the lower-middle class segments. The middle class is estimated to comprise 62% of the population, having grown by 47 million in the past three years (fig.2).

### CONSUMER PROFILE

There are four significant behavioural differences within each socio-economic class. The upper class can be divided into the higher and the upper middle sub-economic class to differentiate behavioural patterns. Unlike more developed countries, which have more uniformity in behaviour, consumers in Indonesia have more diverse preferences. As such, engagement channels that introduce the product or service, variety of product price and quality, and buying channels, vary widely for each social class (fig.3).

### GOLD BUYING BEHAVIOUR

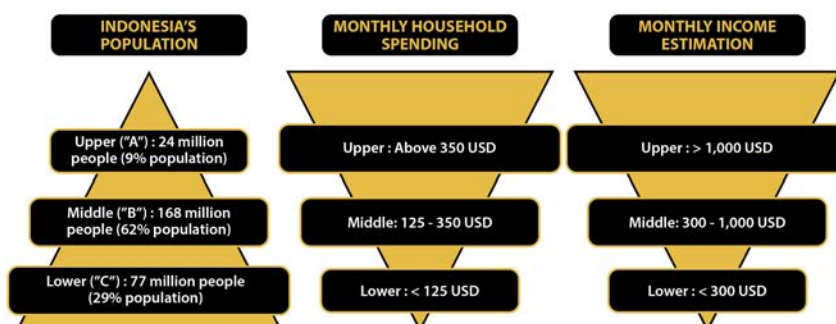
According to Metals Focus, Indonesia's gold jewellery market size reached 40 tonnes in 2018. Gold jewellery purchases among consumers fall into two categories: investment and fashion. Gold jewellery with cubic zirconia stones are popular in Indonesia, as the lower and middle classes cannot afford diamond jewellery, but want a similar look. While the gold consumption figures of each social economic class is not known, the figure for the lower class can be biased as the same product can have a turnover of six to eight times among retailers and consumers (fig.4)

Upper class consumers typically choose 99.99% fine gold bars for investment and diamond jewellery as their main fashion purchase. They also buy plain gold jewellery, usually 18K, in the form of curb chain necklaces, chokers, and hoop earrings. In contrast with the upper class, the lower class segment combines investment and fashion purchases, and has a preference for 8K–10K gold jewellery, followed by cubic zirconia jewellery with the same range of gold content. The behaviour of the middle class segment is a hybrid of the upper and lower class. They have a preference for cubic zirconia jewellery with gold content in the range of 17K–18K. However, for big occasions such as weddings, they usually buy the most affordable diamond wedding rings (fig.5).

### MARKET CHALLENGE

The gold jewellery industry in Indonesia is still considered a blank canvas compared to other consumer-focused industries. The biggest challenge in the gold industry is the lack of standardisation of gold content, with

Figure 2 : Indonesia's demographics



Source: Various Sources of Internal Market Research, 2019

Figure 3 : Indonesian consumer profiles

	A+ (HIGHER)	A (UPPER MIDDLE)	B (MIDDLE)	C (LOWER)
<b>Who am I &amp; How I live</b> Demographics Place to stay, travel	<b>Resident of big cities</b> • World traveller	<b>Residents in the city</b> • Domestic traveller	<b>Spread over the city</b> • Rarely traveling for holidays	<b>Low income, living in the countryside</b> • No traveling
<b>Financial Management</b> Savings Spending	<b>Macro-manage</b> • No certain financial budget • More saving and investing • Minimum debt	<b>Investing</b> • Rough budget with good flexibility • Saving and investing well • Have certain debt	<b>Disciplined financial management</b> • Accurate financial budget with some flexibility • Less investing and saving • Have certain debt	<b>Very tight financial management</b> • Struggling with fulfilling family's needs • No saving
<b>How to engage</b> Media Influencers	<b>Social Media and Celebrity</b> • Barely watch TV and very involved in the digital world • Celebrity trend		<b>Celebrity and Friends</b> • Already involved in digital world with celebrity's life as the focus of attention • Believe in community's recommendation	<b>TV, Store Owner</b> • Often watching TV • Store owner
<b>Favourite products/services</b> Services Product and Brand Lifestyle	<b>Super premium &amp; premium</b> • Shopaholic • Quality	<b>Premium and middle level</b> • Above average • Famous brand • Quality	<b>Middle Level</b> • Average way of life • Good product with reasonable price	<b>Bottom Level</b> • Price sensitive • Not loyal with brand
<b>Buying Behaviour</b> Buying Channel	<b>Exclusive Channel</b> • Prefer an exclusive channel with high value of money • High penetration with new trend	<b>Show Channel</b> • Shop anywhere • Good penetration with new channel	<b>Modern trades</b> • 70/30 modern trade (including minimarket channel) and traditional trade • Start engaging with digital channel	<b>Traditional trades</b> • 30/70 modern trade and traditional/open trade

Figure 4 : Gold purchase behaviour by economic class

Social Economic Class	Purchase Objective	Product Type	Purchase Frequency per Year	Budget Allocation per Year (USD)	Purchase Size for each GOLD Jewellery purchase (USD)
Upper	Investment	Fine Gold Bar 99.99% > 10 gram	1x - 3x	\$1,400 - 7,000	
	Fashion				
	Daily	1) Diamond Jewellery 2) Plain Gold Jewellery	3x - 4x	< \$2,000	• Older : > \$500 • Younger : \$200 - \$500
Middle	Investment	Fine Gold Bar 99.99% 5 - 10 gram	1x - 3x	\$700 - \$1,400	
	Fashion				
	Daily	Gold with Cubic Zirconia ("CZ") Stone 3-10 gram Occasion 1) Diamond, 2) Gold with CZ > 5 gram	2x - 3x	< \$1,400	• All : \$150 - \$300
Lower	Investment	Plain Gold	1x - 3x	\$200 - 700	
	Fashion				
	Daily	1) Plain Gold, 2) Gold with CZ 1-3 gram Occasion Gold with CZ > 3 gram	1x - 3x	\$200 - 700	• All : < \$150

Source: Various Sources of Internal Market Research, 2019



Figure 5 : Example of gold jewellery with cubic zirconia stone



the majority of gold jewellery distributed across the country containing less gold than their manufacturers claim. In 2020, authorities will introduce a national standard reference for gold jewellery content from 8K to 24K. However, much remains to be done in terms of implementation, as the standard will only be a guideline and not mandatory. In addition, enabling infrastructure, such as an independent institution to monitor gold content that can be used by gold shop owners and small-medium-enterprise gold entrepreneurs across the countries, is not available.

Another unique trait is the high buy-back rate of gold jewellery in Indonesia, particularly

among gold shops that serve the lower class segment. Consumers in this segment trade in their gold jewellery more frequently (i.e. monthly or weekly). Such behaviour makes the business model for gold retailers more akin to that of a pawnshop than a commercial trade shop, as 50–80% of the products they sell return to them in a short period of time.

The third challenge – especially pertinent to manufacturers – is providing products with a wide range of gold content, as different regions have varying product preferences. For example, Java – an island that is home to 52% of Indonesia's population – has 8K, 9K, and 10K gold jewellery for the lower class and 17K (yellow gold) and 18K (white gold

and rose gold) for the middle class. However, 20K gold jewellery is preferred on islands such as Borneo (Kalimantan) and 21K gold jewellery is preferred in Celebes (Sulawesi).

In summary, Indonesia is a promising country with a huge business opportunity, including in the gold jewellery sector. However, knowing how to engage with consumers across all touch points and having strong relationship with stakeholders, from the government to the small retailers across all geographies, are critical to growing the business sustainably in this emerging market.

## BUILDING A BRAND

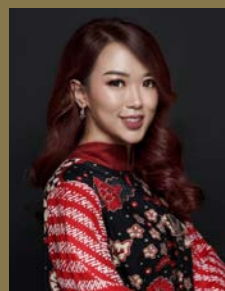
As the newest gold jewellery player in Indonesia, SKK Jewels has been welcomed by all industry stakeholders in the country. We take pride in our Hala Gold brand, which is built following our principles of being honest, authentic, lasting, and aspirational. As the first and the only gold jewellery manufacturer in Indonesia with certified gold content from the Ministry of Industry, SKK hopes to pioneer good industry practices. With this certification, SKK can put the Indonesian National Standard (SNI) mark on all our collaterals, which goes a long way to fostering trust in our brands. We also focus on producing innovative and authentic designs, and strictly prohibit our factories from producing counterfeit products or copying the designs of other factories.

SKK aims to provide a lasting product for our consumers. Our product craftsmanship has been recognised for its quality, which has been compared to diamond jewellery. We maintain high standards of quality control to ensure our gold jewellery products stand out from the competition. This has been a key success driver for our brands, and has allowed the public to acquire 18K gold jewellery with high craftsmanship at affordable prices.

Our last innovation, considered a breakthrough in Indonesia's gold jewellery industry, is in creating an aspirational brand with a unique

identity and precise consumer targeting. We have partnered with top local celebrities to grow our brands over its lifetime, which has created high brand awareness and trust from consumers. Our limited edition series have also created high demand and hype among retailers and consumers. As a result, the organic #HalaGoldHunter movement has grown among consumers who are fans of our products and appreciate our brand values.

Strong engagement from authorities, retailers, trendsetters and consumers, who have also become our advocates, are helping us educate the public on the importance of standardised gold content and high-quality gold jewellery products. This mutually beneficial ecosystem works for the greater good, and will only help develop and grow Indonesia's gold jewellery industry even further.



**JENNIFER HERYANTO** is the founder and Chief Executive Officer of SKK Jewels, a gold jewellery manufacturer in Indonesia and subsidiary of CMK Group, Indonesia's biggest diamond jewellery retailer. She led SKK to be the first and the only gold jewellery factory certified by the Indonesia government for trusted gold content. The company has two champion brands – Hala Gold and Sandra Dewi Gold, a partnership with a leading celebrity Sandra Dewi. Heryanto was previously a business leader in the consumer goods and beauty sector.

# KOREA'S GOLD & JEWELLERY MARKET

BY DA YOUNG KIM, Senior Researcher, Wolgok Jewelry Research Center

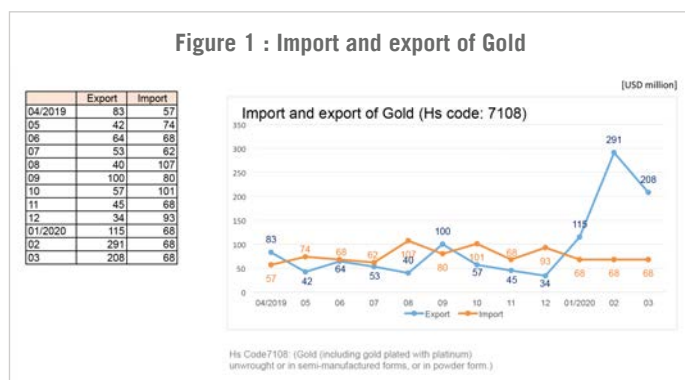
South Korea is a dynamic and innovative country, and its economic growth in the last four decades has been led by its cutting-edge semiconductor industry. The country is also the world's 12th largest economy and Asia's fourth largest, in terms of GDP.

According to the World Gold Council (WGC), South Korea ranks 35th globally in terms of gold holdings, at 104.4 tonnes.<sup>1</sup> This amounts to about US\$4.79 billion, and the market value of gold reserves for the total foreign exchange holding rate is merely 1.3%.

According to Gold Fields Mineral Services (GFMS) South Korea ranked seventh globally in terms of total demand for gold fabrication (including the use of scrap), up 1.4% year-on-year in 2018 at 80.9 tonnes.<sup>2</sup> According to the latest data from the South Korean government, as of the 2018 announcement, approximately 98 tonnes of gold were supplied: 41 tonnes for gold jewellery manufacturing, 38 tonnes for industrial use (PCB, semiconductor, electrical and electronic devices), 16 tonnes for investment gold, and 1 tonne for medical devices. Compared to 2013, the demand for gold investment grew from 5.5 tonnes per year to 16.6 tonnes in five years on the back of its growing importance among investors as a safe haven asset, and investment demand for gold is expected to rise even more in the future.

## GOLD MARKET

According to data from the Korea International Trade Association (KITA) gold exports in February 2020 reached US\$291 million, the largest in seven years, amid high gold prices.<sup>3</sup> On the other hand, gold imports for the same period stood at US\$68 million. The recent sluggish exports in the semiconductor and major manufacturing sectors have recorded a surplus in all gold excluding coins, trade balance (US\$223 million) (fig.1).



Source: Korea International Trade Association

The growing uncertainty worldwide caused by the Covid-19 pandemic has resulted in stronger demand for gold, which has affected the South Korean gold market. The price of gold averaged 173,583 won per gram (US\$38/g) in 2018, but began to rise in August due to global economic uncertainty and a prolonged trade war between the United

States and China in the third quarter of 2019. Average monthly gold prices closed at 200,853 won (US\$44/g) in 2019. Meanwhile, the price of gold, which emerged as a safe asset due to the pandemic, also temporarily went south. But recently, as central banks, including the US Federal Reserve Bank, took active measures to stimulate the economies and economic distress prompted the preference for safe assets, international gold prices rose again to a record 240,803 won (US\$53/g).

According to 2Q 2019 data from GFMS, global gold investment decreased 7% year-on-year, but demand in South Korea grew by 30% (from 4.6 to 6 tonnes). As market uncertainty mounts, the demand for safe haven investments such as gold bars is gradually rising. And silver bars are in short supply too, not to mention mini gold bars (3.75 g, 18.75 g, and 37.5 g). Amid concerns about the global economic downturn, it is expected that the price of gold and the demand for gold bars will continue to grow.

## JEWELLERY

The South Korean jewellery market has high growth potential, as it is a high-value-added industry based on skill-intensive features driven by sophisticated workmanship and high-quality manufacturing. It is also highly likely to converge with the increased global demand for Korean culture. South Korea is ranked seventh globally in terms of gold jewellery manufacturing quantity, with 40.2 tonnes. According to Euromonitor, the South Korean luxury market grew 5.8% year-on-year to US\$23.7 billion in 2018, of which the luxury jewellery market was valued at about US\$1.6 billion, accounting for about 7.8% of the entire luxury market.

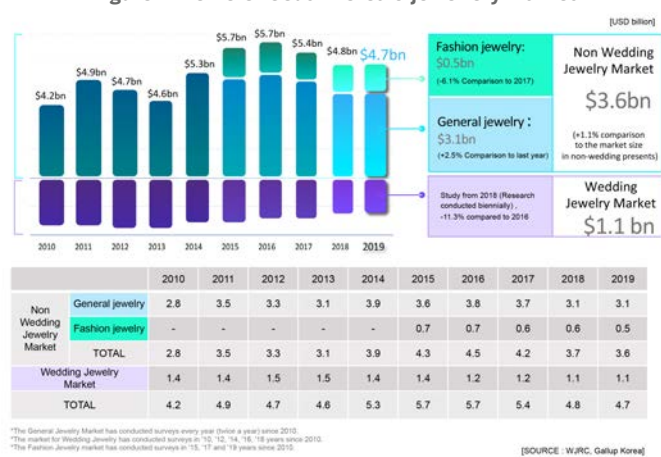
The total number of precious metal jewellery businesses in South Korea is 15,557, with approximately 11,000 retailers, 1,600 manufacturers and 2,200 wholesalers in operation. Some observers say the market itself is somewhat small because private businesses account for 92% of the total. However, it can be regarded as a stable market, given that the numbers of companies and employees have not changed significantly for a decade, and that 20-something-year-old businesses account for 25%.

GFMS reported that as of 2Q 2019, global quarterly gold jewellery consumption fell by an average of 11% compared to the previous year, and that of South Korea also decreased by 12% compared to 4Q 2018 (from 10 tonnes to 8.8 tonnes).

The Wolgok Jewelry Research Center (WJRC) estimated the size of the South Korean jewellery market to be worth some US\$4.7 billion in 2019, 0.8% more than the year before.<sup>4</sup> The wedding jewellery



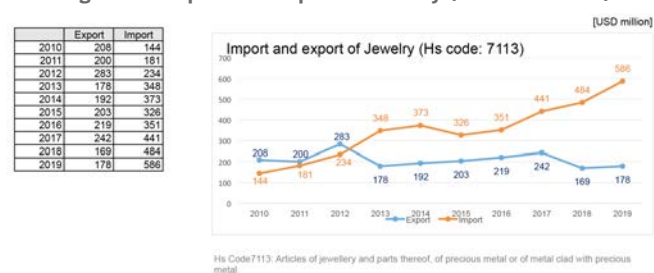
Figure 2 : Size of South Korea's jewellery market



Source: WJRC, Gallup Korea

market, which occupies 22% (US\$1.1 billion) of the market, shrank by 11% compared to 2016 because of a fall in the number of marriages. The size of the non-wedding jewellery market, which accounts for 78% of the total, was estimated at US\$3.6 billion (1.1% growth) (fig.2).

Figure 3 : Import and export of Jewelry (Hs code: 7113)



Source: Korea International Trade Association

Unlike gold exports, South Korea's jewellery exports keep running record-breaking trade deficits annually. As of 2019, exports were up 6% from the previous year to some US\$108 million, but imports during the same period increased by 21% year-on-year to some US\$590 million, up 306% over the past decade. This is linked to the aforementioned growth of the luxury jewellery market (fig.3).

The consumption of gold jewellery, which takes the lion's share of the total gold market in the country, is closely related to the domestic economy. The low-growth trend has been evident since 2016, which has affected both general gift/self-adornment and wedding jewellery markets, throwing the jewellery industry into jeopardy. Consumption and sales have continued to decrease due to the contracting domestic economy.

The biggest recent change that has affected the South Korean gold and jewellery market is the change in tax laws. The country banned the import of luxury goods (furs, bags, and watches including gems and jewellery) until 1990, and then started to allow imports but with an introduction of the Special Consumption Tax (SCT) to discourage consumption of goods priced over a certain amount, which varied by item and by year on top of general VAT (currently 10%) and import tax. In 2015, SCT was 20% and another 6% education tax was levied on SCT-applicable items. This resulted in a tax-heavy system that caused the black market to proliferate. Thus, it is not easy to estimate how much gold the Korean public is holding.

Moreover, as more than 90% of precious metals and stones, the main raw materials for gem-set jewellery, were imported, the SCT took away price competitiveness from the production cost. It served as a major impediment to growth not only for the domestic market but also for the export-led sector. In addition, even though South Korea signed free trade agreements (FTAs) with 55 countries, it was difficult to prove the origin of the product to benefit from the FTAs.

As a result of lobbying by local jewellery industry players, the country revised two key laws (SCT Act and Customs Act) three times from 2015–2019 to liberalise the industry and strengthen its competitiveness on the global stage. In 2015, after the first revision of the Special Consumption Tax Act, the threshold for SCT on gems and jewellery rose 20% (another 6% education tax extra) from 2 million won to 5 million won, and retailers were excluded from this tax payment. The SCT on gem (diamonds and coloured stones) imports was completely lifted in the second revision of the act in 2018, and the tariff on loose stones used for gems was removed on April 1, 2020 (fig.4).

The domestic market is not expected to recover quickly amid rising gold prices due to the coronavirus outbreak, poor consumer sentiment and shrinking industrial output caused by a sluggish domestic economy and risk of falling into a long-term global recession. However, the local gold and jewellery industry players are hoping the revised law will help revitalise the domestic market and jewellery export business.

Figure 4 : Tax system revisions in Korea

Category	Tax base	Tax rate
<b>Special Consumption Tax (SCT)<sup>1</sup> = 20% + 6% education tax extra = 26%</b>		
~Feb 02, 2015	Luxury goods (furs, bags, and watches including gems and jewelry...)	Not more than KRW 2 million (USD 1,641)/ea: 0% Over KRW 2 million (USD 1,641)/ea: 26%
1th Feb 02, 2015	Gems (Diamond & Colored Stone) & Jewelry	Not more than KRW 5 million (USD 4,102)/ea: 0% Over KRW 5 million (USD 4,102)/ea: 26%
	Luxury goods (furs, bags, and watches ...)	Not more than KRW 2 million (USD 1,641)/ea: 0% Over KRW 2 million (USD 1,641)/ea: 26%
2th Dec 08, 2018	Gems (Diamond & Colored Stone)	Exempt: 0% Over KRW 5 million (USD 4,102)/ea: 26%
	Jewelry (Precious metal products)	Over KRW 5 million (USD 4,102)/ea: 26%
	Luxury goods (furs, bags, and watches ...)	Over KRW 2 million (USD 1,641)/ea: 26%
<b>Import Tax (IT)</b>		
~Dec 27, 2019	HS CODE :71 <sup>2</sup>	rough stone (diamond for industrial use and raw ore): 1% Gems (Diamond & Colored Stone): 5% Jewelry (gold & fashion jewelry): 8%
3th Dec 27, 2019	HS CODE :71	rough stone (diamond for industrial use and raw ore): Exempt Gems (Diamond & Colored Stone): Exempt Jewelry (gold & fashion jewelry): 8%

\* VAT 10% EXCLUDED \*

<sup>1</sup> The Special Consumption Tax (SCT) shall be levied on specific goods, admission to specific places, entertaining, eating, and drinking at specific places, and business activities at specific places. [https://elaw.kiri.re.kr/eng\\_service/lawView.do?hseq=40919&lang=ENG](https://elaw.kiri.re.kr/eng_service/lawView.do?hseq=40919&lang=ENG)

<sup>2</sup> Chapter 71 Natural or cultured pearls, precious or semi-precious stones, precious metals, metals clad with precious metal, and articles thereof, imitation jewellery, coin

<sup>3</sup> Value-added tax (VAT). Consumption taxes: All corporations and individuals that supply goods or services, regardless of whether for profit or not, are subject to 10% VAT. VAT is levied on supplies of goods and services, and on the import of goods into the country.

## Notes

<sup>1</sup> World Gold Council, <https://www.gold.org/>

<sup>2</sup> Gold Fields Mineral Services, <http://solutions.refinitiv.com/MetalsResearch>

<sup>3</sup> Korea International Trade Association (KITA), <https://www.kita.net/>

<sup>4</sup> WJRC (Wolgok Jewelry Foundation), <https://w-jewel.or.kr/wjrc>



**DA YOUNG KIM** is a senior researcher at Wolgok Jewelry Research Center, a non-profit organisation and subsidiary of Wolgok Jewelry Foundation established in 2009 to support Korea's gold and jewellery industry, and engage in market and consumer research. Da Young's research focuses on the jewellery market structure, legal system, and government policy.

# GOLD RUSH 2.0: AUSTRALIA TO BECOME WORLD'S BIGGEST GOLD PRODUCER

BY SHAE RUSSELL, Chief Editor, *The Daily Reckoning Australia*

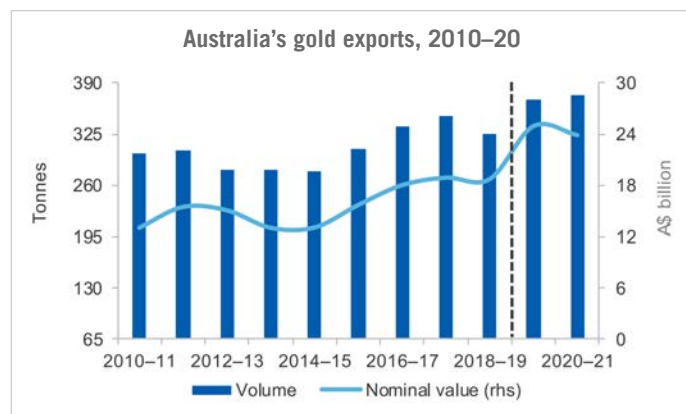
The price of gold is starting to stretch its legs. But years of underinvestment in both exploration and mine expansion mean that many miners around the world are at risk of having little left to dig up. When the gold price falls, exploration is the first thing to go from the budget. Yet it can take a decade or more to turn a gold find into a gold mine.

Rising prices mean we're prepared to pay top dollar for precious metals. But globally, gold miners didn't build their resources when the price was low. By underinvesting in exploration, they've hurt future production and are missing out on a once-a-century opportunity.

Next year, Australia will be the world's largest gold producer, producing an estimated 383 tonnes of gold, and will knock China off the top spot it's held since 2007.<sup>1</sup>

One estimate for the Middle Kingdom says that growth will be stagnant over the next decade, suggesting that Russia will overtake the country and bump it all the way down to number three.

Australia didn't become number one by accident though. Currency parity with the US dollar back in 2010–11 meant some gold miners were losing money. This brief moment, when one Aussie dollar was worth more than one greenback, forced Australian gold miners to become lean producers. Not only did Aussie gold miners cut the bloat from the budget, they streamlined processes to produce more gold for less cost.



## GOLD-RICH

Australia's 17% of economically demonstrated resources (EDR) is 5.6 times higher than China's 3%. In fact, Australia's gold reserves are larger than in Russia or South Africa. Australia's known gold deposits are even larger than the US and Canada's reserves combined.

The stories of how gold mining emerged in Australia pretty much involves stumbling upon the shiny rock: a nugget was found in a riverbed in a place called Poverty Point. Once word of this nugget spread, the 1850s gold rush began. On the west coast in the 1890s, a horse kicked over a rock and gold was found. This very spot went on to house Australia's longest running gold mine, pouring gold for 120 years.

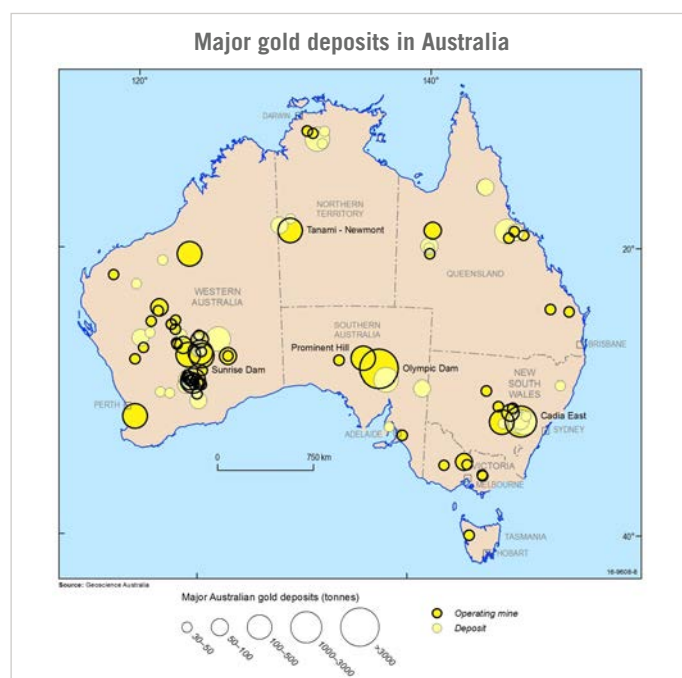
The ease of finding gold has much to do with Australia hitting the geological jackpot. We are literally peppered with gold deposits. Some

**ONE OF THE UNIQUE FEATURES OF THE AUSTRALIA'S GOLD MINING INDUSTRY IS THAT EVERY SINGLE STATE HAS GOLD RESERVES AND IS ACTIVELY MINING GOLD.**

places have richer gold plots than others. One of the unique features of the Australia's gold mining industry is that every single state has gold reserves and is actively mining gold.

Western Australia has about 43% of economically demonstrated resources (EDR), yet this state produces a mammoth 70% of the country's total gold. While Western Australia is famous for its Super Pit (a joint venture between Saracen Holdings and Northern Star), it is only Australia's second biggest producer of gold.

Top spot goes to Boddington (Newmont Corp), which is located 120 kilometres from Perth and pours a whopping 741,000 ounces of gold per year on average. Newmont Corp owns another big gold producer in the Northern Territory (4% of EDR) – the Tanami mine, which produces 500,000 ounces annually.



Source: Geoscience Australia



However the biggest gold miner by ounces is the copper gold porphyry Cadia mine operated by Newcrest Mining in New South Wales (18% of EDR), which sent some 871,216 ounces to market last year. Newcrest is out to make Cadia an even bigger miner, increasing production from less than 28 tonnes (900,000 troy ounces) of gold in 2019, to a mammoth 35 tonnes (1,125,000 ounces of gold) of gold by 2023.

Head a little further south and you'll find one of the richest gold mines in the world.

The Fosterville mine (Kirkland Lake Gold) is the largest gold producer in Victoria (1% of EDR), pouring 619,366 ounces in 2019. While it doesn't produce as much as others, the transformation at Fosterville is reviving the Victorian gold mining industry.

Fosterville is smack in the guts of the first Australian gold rush. By simply digging deeper, Fosterville has become one of the highest gold grade mines in the world, with an average grade of 39.6 grams per tonne.

## EXPLORATION CRUCIAL FOR SUCCESS

Mining is an odd business. Your greatest asset is a depleting one. An ounce out of the ground is an ounce out of the ground. In spite of how important it is to secure a future resource, exploration is the first thing to go when the price of gold dives.

**SUCCESSFUL EXPLORATION TODAY  
MEANS INCREASED GOLD PRODUCTION  
A DECADE FROM NOW.**

Global exploration expenditures peaked when the gold price hit an all-time high, as the price fell so did the money spent looking for it. This short-sighted thinking from miners hinders future production. Successful exploration today means increased gold production a decade from now.

Aussie miners are in an enviable position right now. The weakening Aussie dollar is pushing the Aussie dollar gold price up. Higher prices not only encourage increased production, but creates an incentive to spend big and go looking for more.

As it stands, Australia is one few gold producers with exploration spending back to 2012 levels. Nevertheless, it has to be this way as gold is becoming increasingly harder to find.

The last tier 1 or giant discovery in Australia was the Tropicana deposit in 2005. However, Australia isn't alone – giant discoveries of almost any commodity are almost non-existent. There are two reasons for this: lack of spending on exploration and having to look harder. The easy gold at the surface has been found.

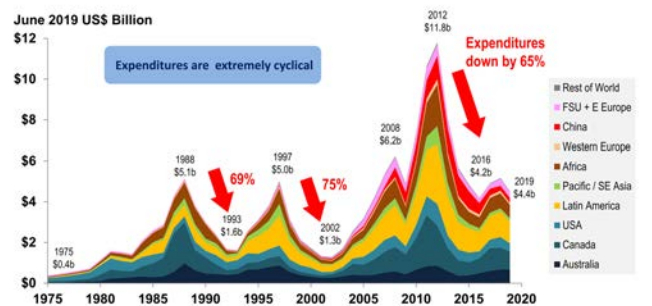
Australia, and many other gold producing nations, must spend more money than ever before to find gold. To ensure efficiency, exploration programs will need to be carefully targeted. "Nearology" may be successful for existing mines. Yet greenfield sites will need extensive geophysics before any drilling can begin.

This will be expensive, but once again luck strikes Australia. Here the average depth from surface for a discovery is quite low. The average depth for a brownfield site in the Lucky Country is just 299 metres, compared to the US, where it is 415 metres.

**THERE HAS BEEN A PERSISTENT  
UNDERINVESTMENT AND  
MISINVESTMENT IN GOLD EXPLORATION  
AROUND THE WORLD.**

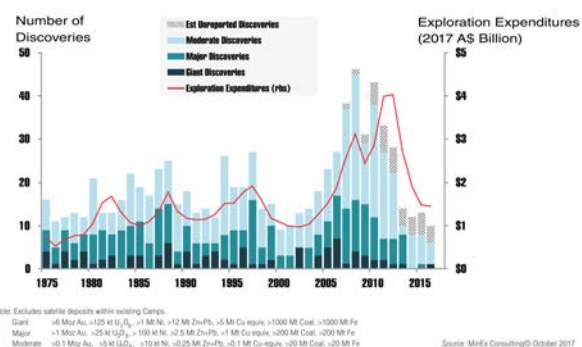
It is a similar story for greenfield sites. A new find in Australia is on average only 30 metres from the surface and in the US the average greenfield site begins another 10 metres on top of that.<sup>2</sup>

## Global gold exploration expenditures 1975–2020



Source: MinEx Consulting

## Global outlook: Number of discoveries correlate with exploration spending



Source: MinEx Consulting

High gold prices encourage deeper exploration, but perhaps this isn't the answer to securing more gold. Technology advances can drastically alter commercial viability of a mine. The next giant discovery may not come from exploration, rather a change in what's an economical project.

Carbon in pulp processing was a revolution for American gold miners in the 1970s, and as a result was commonplace in Australian mining by the 1980s. This was a game-changer for the industry. Low gold grade deposits could now be processed. This technology not only transformed what could be mined, it set Australia up to become the dominant supplier of gold it is today.<sup>3</sup>

There has been a persistent underinvestment and misinvestment in gold exploration around the world. Australia has been well prospected, but not well explored. Higher gold prices and technology advancement could see Aussie gold miners prosper well into the 2020s.

### Notes

- Department of Industry, Science, Energy and Resources, Commonwealth of Australia. Resources and Energy Quarterly (March 2020).
- Gold Industry Group, "The Future Looks Bright for Gold" (October 2019) retrieved from: <https://www.goldindustrygroup.com.au/news/2019/10/8/req-report-the-future-looks-bright-for-gold>
- Bill McKay, Ian Lambert and Shige Miyazaki. "The Australian Mining Industry: From Settlement to 2000", Australian Mining Industry, 1998-99 (Australian Bureau of Statistics, cat. no. 8414.0).



**SHAE RUSSELL** is the chief editor of The Daily Reckoning Australia, where she breaks down global macro-economic trends for Australians, and is Fat Tail Media's leading analyst on bullion and precious metal miners.

# SPECIAL FOCUS: JAPAN BULLION MARKET ASSOCIATION

BY BRUCE IKEMIZU, *Chief Director, Japan Bullion Market Association*



JBMA's launch party on October 29, 2020, in Tokyo, Japan

## REVIVING JAPAN'S PRECIOUS METALS SECTOR

The Japan Bullion Market Association (JBMA) was formed in September 2019. This was not long after I left the bank where I had worked for the past 13 years, following its decision to close the bank's Tokyo branch. Along with colleagues working in the industry, I had long been planning to contribute to the development of Japan's precious metals market. From what I have seen in my experience in the Japanese gold market over the past three decades, the market has regrettably lost its energy during this time, particularly when compared to the gold and precious metals trading heydays of the 1980s, 1990s and 2000s. Back then, Japan, which has a very active Tocom futures market, was surely an Asian gold trading hub.

As a trader and as market participant, I had long been thinking about how I could help revive the Japanese precious metals market. The establishment of JBMA is a good opportunity for Japan's precious metals community to do just that. The country's precious metals market is currently vertically segregated between physical metals traders, such as smelters, recyclers and retail bullion shops, and financial firms that are trading gold contracts for difference (CFD), futures contract brokers, banks and security houses that are involved in precious metals exchange-traded funds (ETFs). JBMA is trying to fill the gap in the gold industry from physicals, futures, and financials. To us, gold is gold, whether it is in the form of physical kilobars, gold coins, ETFs or futures contracts. There must something the different sectors of the gold market can do together to promote precious metals to Japanese investors and people on the street. JBMA is ready to build bridges between those parties for the good of the precious metals industry as a whole.

JBMA has started by focusing on investor educations on precious metals. We have conducted several seminars to investors in several cities, and have set ourselves a target of conducting grassroots seminars in all 47 prefectures in Japan. Unfortunately, the Covid-19 pandemic has put a hold on our outreach efforts for the time being. Before the quasi lockdown that has been enforced in Japanese cities, we had already started to conduct seminars online, inviting

specialists from all over the world to speak on not only precious metals but also other related areas like foreign exchange, equities, emerging markets, and more. This has proved to be a very useful channel of disseminating information as within a month, we have already reached over 10,000 viewers. SBMA CEO Albert Cheng spoke about the situation in Singapore and how Covid-19 is affecting the gold market in Southeast Asia in two of such sessions.

JBMA has received strong support from our associate cooperate members, which include Japan Exchange (JPX) – the biggest exchange group in Japan, which will merge Tocom precious metals contracts from July 2020 – as well as the World Platinum Investment Council (WPIC), Bullion Vault and Gold News. JBMA is offering JPX members educational programs on their contracts. More than 300 traders and sales executives from JPX member companies, such as trading houses, mining houses, banks, security houses and futures commission merchants attended our three-day intensive online course in mid-May. We are also helping WPIC to market platinum and palladium investment in Japan by translating their research and publications into Japanese and circulating them among Japanese investors.

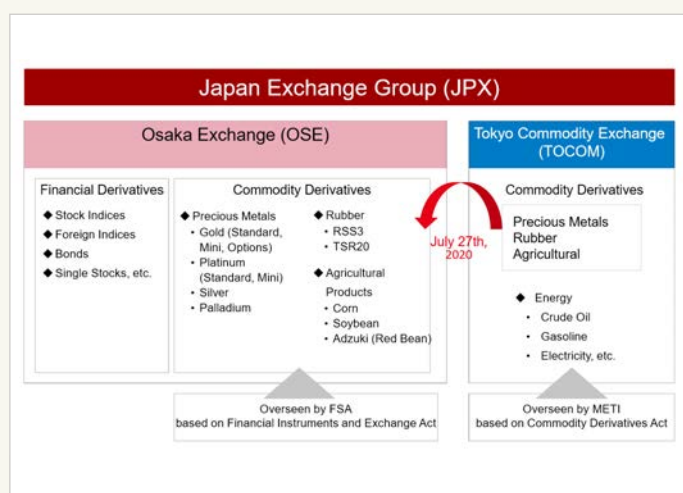
As information in Japanese that compares platinum group metals (PGM) with gold is scarce, these reports have been well-received and are helping to boost the interest in PGM among investors. We are also connecting Japanese corporates who are involved in PGM investment to WPIC and are helping Bullion Vault reach Japanese investors with their products. Soon, we hope to sign with SBMA a memorandum of understanding that covers market development between Japan and Southeast Asia.

We are still not clear what kind of world will emerge after Covid-19 – we don't even know if there will be an "after" at all, but we will adjust ourselves to this reality as it changes as we are certain the value of precious metals will be much higher in this unseen future.



# CHANGES COMING TO JAPAN'S COMMODITY FUTURES MARKET

The Japanese commodity futures market is ripe for change. Historically speaking, the global futures market traces its origins to Japan in 1730, with the establishment of the rice futures exchange in Dojima City, Osaka. The Tokyo Commodity Exchange (Tocom) has its roots in Dojima. It started as the Tokyo Gold Exchange in 1982 and merged with the Tokyo Textile Exchange and Tokyo Rubber Exchange in 1984 to become Tocom as we know it today. The bourse grew its precious metals trading each year, with gold open interest peaking in February 1996 at 617 tonnes. Unfortunately, this volume steadily declined in recent years to 61.7 tonnes – exactly 1/10th of its peak, while open interest on Comex is now 1,632 tonnes. However, in the past three decades, Tocom has been the most active and important precious metals futures markets in Asia, closely trailing Comex/Nymex globally.



## List of JPX Commodity Derivatives Products

●JPX offers diversified commodity futures and options contracts, ranging from precious metals, energy, rubber to soft commodities.

<b>Precious Metals</b>	<ul style="list-style-type: none"> <li>Gold (Standard, Mini, Options)</li> <li>Silver</li> <li>Platinum (Standard, Mini)</li> <li>Palladium</li> </ul>
<b>Energy</b>	<ul style="list-style-type: none"> <li>Platts Dubai Crude Oil</li> <li>Gasoline</li> <li>Kerosene</li> <li>Gas Oil</li> <li>Chukyo Gasoline</li> <li>Chukyo Kerosene</li> <li>Electricity (Base load, Peak load)</li> </ul>
<b>Rubber</b>	<ul style="list-style-type: none"> <li>Ribbed Smoke Rubber (RSS3)</li> <li>Technically Specified Rubber (TSR20)</li> </ul>
<b>Agricultural Products</b>	<ul style="list-style-type: none"> <li>Corn</li> <li>Soybean</li> <li>Adzuki (Red Bean)</li> </ul>

Tocom has been an independent commodity futures market for precious metals, energy, rubber and agricultural products. Market participants and investors, however, recognise that this alone cannot sustain the exchange. For more than 10 years, the government and private sector have been studying the possibility of making it a comprehensive exchange, which covers stocks, financial derivatives and commodities under one umbrella, but the idea has not materialised because of the interests of the supervising ministries (i.e. Financial Services Agency, which governs financial instruments, and the Ministry of Trade and Ministry of Economy, Trade and Industry which covers commodities).

The battle over the governance of the new comprehensive exchange, which would include both financial instruments and commodities, was finally solved in October 2019, when Japan Exchange Group (JPX) conducted a tender offer for the issued shares of Tocom and converted Tocom into a wholly owned subsidiary of JPX.

JPX is the biggest exchange group in Japan and it has Tokyo Stock Exchange (TSE), the biggest stock market in Japan and Osaka Exchange (OSE), which specialises in financial derivatives. With Tocom under its umbrella, it is making some structural changes as a new comprehensive market.

From July 2020, some contracts will be transferred from Tocom to OSE, including precious metals contracts (gold, silver, platinum and palladium), rubber and soft commodities (corn, soybean and red bean). Only energy and electricity contracts will remain under Tocom. With this move, the Financial Services Agency will become the supervising ministry. More importantly, stock market investors who never had a chance to trade gold or other precious metals will have significantly easier access to this market.

The number of Japanese investors in the commodities futures market is estimated to be 100,000, which was the limit we had for a long

time. For the commodities market, and gold in particular, this is a significant opportunity to broaden the investor base. Compared to the stock market, the commodities market is small. A small share of equities investors would change the gold market completely.

JPX has joined the Japan Bullion Market Association (JBMA) in April, and together, we have conducted intensive educational training for sales representatives and traders from security houses who have not had any experience in the commodities market. We are also planning an extensive education campaign for investors relating to the contract transfer in July. With the Covid-19 pandemic putting our roadshow to all 47 prefectures on hold, we are now conducting out outreach activities online.

With the gold price currently at a 40-year high in Japanese yen, there is a huge interest in gold among people on the street. Both JPX and JBMA are working to seize this opportunity, which will hopefully positively impact the precious metals market in Asia and the world.



**BRUCE IKEMIZU** is chief director and precious metals specialist at JBMA. He began his career at Sumitomo Corporation as a gold trader after graduating from Sophia University in 1986. He then worked for Credit Suisse and Mitsui & Co. before joining Standard Bank in 1996. He was the head of Tokyo branch of ICBC Standard Bank until leaving the bank in 2019. Bruce is currently using his knowledge and relationships within the sector to develop and grow the newly formed JBMA.



# GLOBAL OVERVIEW OF PRECIOUS METAL LOGISTICS

BY ALLAN FINN, *Director of Global Commodities, Malca-Amit*

There has been a great deal of excitement around physical stocks of gold and their geographic location since the spread of Covid-19 to the European Union and the United States. From a gold pricing perspective, the biggest single issue has been the disparity between the price of gold in London and New York. There are many theories about what lies behind this.

**THERE HAS BEEN A SIGNIFICANT DROP IN PASSENGER AIRCRAFT FLIGHTS, WHICH ARE TRADITIONALLY UTILISED FOR THE MOVEMENT OF VALUABLES SUCH AS GOLD.**

One event that occurred in the physical market at the time this disparity occurred was the closure of three of the four major Swiss gold refineries, based in the south of Switzerland, and close to the heavily impacted parts of Italy. These closures were short-term and all refineries are now operating and busy.

The second reported factor was the significant drop in passenger aircraft flights, which are traditionally utilised for the movement of valuables such as gold. In the United Kingdom, Gatwick is closed and Heathrow is operating at 33% of its "normal" capacity, while Changi Airport in Singapore has seen a fall in passenger footfall of more than 50%. To the outsider, the immediate conclusion was that this would restrict the ability of secure logistics providers to facilitate the global movement of stocks. This assessment was naïve and ill-informed.

The reduction in passenger air travel has put a squeeze on space, and competition for that space between the various types of cargo that normally utilise it has become fierce with freight prices on some airlines increasing by over 400%. But space can still be secured, which means the decision to move gold becomes a simple profitability test. Can higher logistics costs be reasonably absorbed by potential profits, or by preventing the loss at the final stage of the deal? This, in turn, becomes a decision for our customers to make. Malca-Amit has fulfilled all transportation requests so far during this period and our precious metals departments have had their busiest month in years.

## ADAPTING OPERATIONS

Malca-Amit has also adapted operations to maintain a service that works for our customers. The use of cargo freighters has been necessary and working with the airlines, the company has been able to provide the right level of security to permit some limited use of these assets. The charter of full aircraft has always been a solution in the valuable logistics world, normally reserved for exceptional movements or use in remote areas, and this mode of movement has been utilised on standard lanes where passenger or freighter solutions were unable to provide the necessary capacity.

There is much debate about the immediate future of the aviation industry but what the past two months have demonstrated is that logistics providers can keep pace with a changing environment and as long as there is a global physical market, their contribution is critical.

Our vaulting and safety deposit box network has seen a huge spike in demand as companies look for business continuity solutions or to take short-term advantage in geographical areas where they currently don't have a capability. Our third-party logistics solutions allow our customers to continue to operate while keeping their facilities closed or at minimum manning.

**WHAT THE PAST TWO MONTHS HAVE DEMONSTRATED IS THAT LOGISTICS PROVIDERS CAN KEEP PACE WITH A CHANGING ENVIRONMENT.**

As a transporter that supports the global financial market, Malca-Amit staff are considered key workers, and our teams are able to operate with the correct and safe Covid-19 prevention measures throughout this crisis. They have worked tirelessly to support our customers and maintain the credibility of the precious metals markets and innovate daily to solve issues for our customers.

## RECOVERY EXPECTED

What does the future hold? There will no doubt be a swing back to Asia for flows of precious metals as the current opportunities are met. The post-Covid-19 precious metals world might even see a London Deliverable Kilobar market, who knows? In the short and medium term, it is clear the world will be a little different and will pose new challenges. What we are sure of is that Malca-Amit will be there with our customers every step of the way, adapting, solving, reassuring and delivering absolute peace of mind.

**ALLAN FINN** is the Director of Global Commodities Malca-Amit, a storage and logistics company specialising in precious metals, jewelry, fine art. He has been with Malca-Amit for a decade and has a total of over 15 years of logistics experience.



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# GOLD DEMAND TRENDS AND THE IMPACT OF COVID-19

BY ANDREW NAYLOR, *Head of ASEAN and Public Policy, World Gold Council*

At the end of April, the World Gold Council published its first quarter Gold Demand Trends. Gold demand inched up to 1,083.8 tonnes in Q1, supported by investment (fig.1).

Unsurprisingly, the Covid-19 pandemic has had an impact. It has fuelled safe-haven investment demand for gold, offsetting marked weakness in consumer-focused sectors of the market. Investment demand – driven by economic uncertainty – has resulted in record inflows into gold-backed exchange-traded funds (ETFs) and similar products. As the scale of the pandemic and its potential economic impact started to emerge, investors sought safe-haven assets. Gold-backed ETFs and similar products attracted huge inflows (+298 tonnes), which pushed global holdings in these products to a new record high of 3,185 tonnes.

**COVID-19 HAS FUELLED SAFE-HAVEN INVESTMENT DEMAND FOR GOLD, OFFSETTING MARKED WEAKNESS IN CONSUMER-FOCUSED SECTORS OF THE MARKET.**

This has offset weaknesses in consumer demand, particularly the jewellery market. A combination of lockdowns and consumer uncertainty has seen demand for jewellery fall. Quarterly demand dropped 39% year-on-year to a record low for our series of 325.8 tonnes. Central banks continued to be significant buyers of gold, although at a lower rate than in Q1 2019: net purchases amounted to 145 tonnes (-8% year-on-year).

It is fair to say that the pandemic has had an unprecedented impact. It has disrupted global supply chains, paused large sections of the economy, put huge pressures on governments, and knocked consumer confidence. Higher risk and uncertainty, combined with a lower opportunity cost, will likely be supportive of gold investment demand in 2020. This could continue to offset the negative effect of lower consumer demand on gold performance as economic activity contracts.

It is clear the global economic outlook is highly uncertain, and as governments grapple with deficits and the need to kick-start the global economy, gold will play an ever-increasing role in investment portfolios.

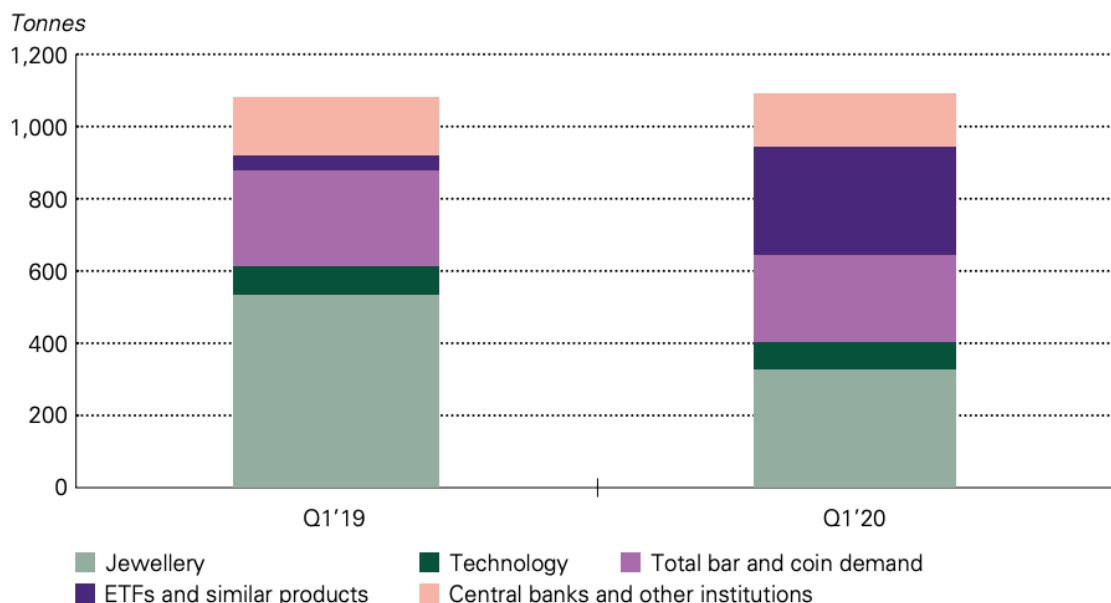
## THE FUTURE

The uncertain economic outlook and the potential for a second wave mean a low-interest environment is here to stay for the foreseeable future. In this environment, investment interest in liquid, wealth-preserving safe-haven assets like gold will grow. For the World Gold Council, this means a lot of our focus will be increasing the understanding wealth managers and asset allocators have of gold. Singapore, as a leading wealth management hub with over \$2.7 trillion of assets under management, is a key nexus in the wealth management ecosystem.

As part of our efforts to increase understanding of gold, last year we launched Qaurum, a web-based quantitative tool that helps investors intuitively understand the drivers of gold's performance by demonstrating how gold may react across different macroeconomic



Figure 1 : Coronavirus ignited safe-haven ETF inflows, but undermined consumer demand



Source: World Gold Council, Gold Demand Trends Q1 2020

environments. In May, we updated the macroeconomic scenarios behind Qaurum to reflect the latest perspectives from Oxford Economics, which include the potential impact of Covid-19 on the global economy.

There is work to be done on the retail side too. Interest in fintech and digital gold products is increasing. Digitally managed products play an important role in democratising access to gold and opening the asset class to the retail market, but best practice must be adopted in this sector so consumers can feel confident in this important market segment. To this end, the World Gold Council has created the Retail Gold Investment Principles – a set of principles for the retail gold market designed to set the bar for product providers and further encourage retail investors to place their trust in gold. It is envisaged that greater trust will benefit customers and product providers alike, creating value and driving demand across the retail gold industry.

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THIS IMPORTANT MARKET SEGMENT.**

We undertook an industry survey earlier this year. The response is being analysed, and a further round of intensive industry engagement will take place later this year. Finally, work continues to address key environmental, social and governance (ESG) issues for the gold mining sector.

#### DRIVING SUSTAINABILITY

Last year we launched the Responsible Gold Mining Principles – a new framework that sets out clear expectations for consumers, investors, and the downstream gold supply chain as to what constitutes responsible gold mining. It is our aim that these principles will

become a credible and widely recognised framework through which gold mining companies can provide confidence that their gold has been produced responsibly.

The Responsible Gold Mining Principles are intended to recognise and consolidate existing standards and instruments under a single framework. Several leading standards already exist that address specific aspects of responsible gold mining, including the United Nations Guiding Principles on Business and Human Rights, the OECD Due Diligence Guidance for Responsible Business Conduct and the Extractive Industries Transparency Initiative, Guidelines for Multinational Enterprises and the International Council on Mining and Metals' (ICMM) Performance Expectations. But before the development of the Responsible Gold Mining Principles, there was no single coherent framework that defined responsible gold mining.

Sustainable finance is growing fast – a recent survey suggested nearly 75% of young Singaporeans are keen to ensure their investments are sustainable. And on the regulatory and market development side, the Monetary Authority of Singapore (MAS) is leading the way to ensure Singapore's financial sector incorporates ESG considerations into financial decisions. Going forward, the World Gold Council will continue to help increase awareness of the work the industry is doing to drive sustainability, and the role that gold plays in sustainable investment portfolios.



**ANDREW NAYLOR** joined the World Gold Council in 2016 and is responsible for the WGC's activities in the region – institutional investment, government relations, and public policy initiatives. Prior to this role, he worked for international consultancy firm Cicero Group advising financial institutions on foreign investment and trade policy in Asia and regulatory reform. Andrew has been a board member of the European Chamber of Commerce in Singapore since 2012 and was chairman of its financial services committee from 2012 to 2014, and treasurer from 2014 to 2016. Andrew has a degree from the London School of Economics and Political Science.



# ROAD TOWARD \$2,000+ GOLD SET TO BE A BUMPY ONE

BY BART MELEK, *Global Head of Commodity Strategy, TD Securities*

Spot gold has more than rebounded from the mid-March Covid-19 driven collapse and is now trading in a range near \$1,700/oz. The yellow metal rallied along with risk assets following the reduction of extreme volatility, after the United States (US) Federal Reserve and other central banks announced measures to provide potentially unlimited support to credit markets and governments around the world provided countless trillions of dollars in fiscal support to keep consumers and corporations solvent.

However, before prices move into a significantly higher range, a drift lower is a significant risk. Somewhat higher real interest rates amid reduced systemic risk, the Fed's commitment to positive policy rates, transitory disinflation, a firm USD, ample availability of physical metal to deliver against Comex futures (which may soften the "gold shortage" narrative, albeit misplaced) and a firm appetite for equities are all reasons why the yellow metal may straddle the lower bound of the trading range before surging higher.

The resumption of a downward trend in real rates, which remain in negative territory, along with a low cost of carry and concerns surrounding fiat currency debasement as skyrocketing debt makes various forms of debt jubilee appealing in some circles, likely mean the gold price could test TD Securities' target of \$2,000+/oz in the latter part of 2021. A normalising global economy and the fraying of global supply chains in the aftermath of the coronavirus crisis likely mean that policy rates will continue to be set below the rate of inflation. This, along with monetisation pressures, as fiscal deficits surge in the US and across the world, should see investors choose the yellow metal as protection.

## ENVIRONMENT NOT RIPE FOR BREAKOUT TO HIGHER RANGE

Gold has rallied along with risk assets, as volatility dropped from record levels, following the end to the dash-for-cash which included aggressive selling of the yellow metal during the worst of Covid-19 market instability. The reversal came after the Fed announced measures to provide unlimited liquidity to support public and private fixed income markets and as the market was convinced the US Treasury and other governments will introduce a stimulus package worth trillions of dollars designed to provide funds to stabilise household and business balance sheets that have been beaten down by the coronavirus outbreak.

After declining for some two weeks, which prompted many investors to question gold's safe-haven bona fides, the metal started to see a resurgence, as the pressures to grow dollar positions eased. Once the funding stresses that drove prices lower alleviated further, as the

**A NORMALISING GLOBAL ECONOMY AND THE FRAYING OF GLOBAL SUPPLY CHAINS IN THE AFTERMATH OF THE CORONAVIRUS CRISIS LIKELY MEAN THAT POLICY RATES WILL CONTINUE TO BE SET BELOW THE RATE OF INFLATION.**

Fed and other key central banks monetise Covid-19 related market dysfunctions and major governments spend trillions of borrowed money to fortify stressed households and corporates, such that liquidity problems don't morph into a solvency crisis, investors pivoted their focus towards gold as a hedge again.

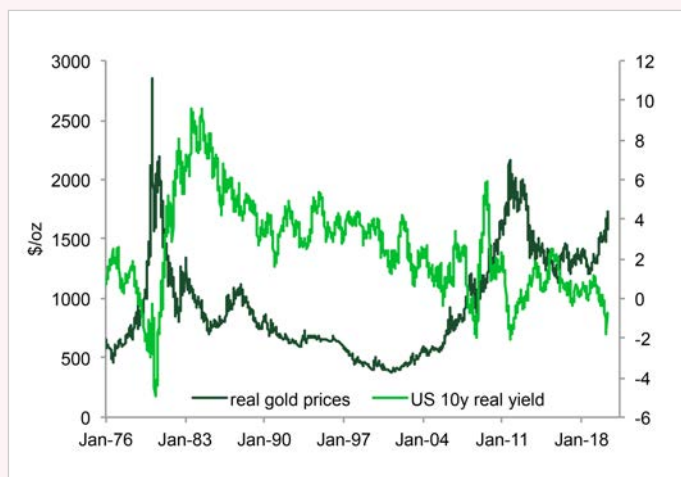
Normalising liquidity conditions, negative real rates, low cost of carry and concerns surrounding fiat currency debasement, not unlike which were present post-global financial crisis period, were all important in generating gold's outstanding performance to make it the best performing major asset class.

However, after a very strong March and April, which saw spot prices surge some 20% off the Covid-19 induced lows, gold has had a few bad days in late April and early May, and has now stalled in a narrow trading range near \$1,700/oz. The recent market disappointments in the policy narrative by the European Central Bank (ECB) and the German Federal Constitutional Court's landmark decision that the ECB's current quantitative easing bond purchasing program conflicts with German basic law was one of the major catalysts prompting a pullback of investor interest away from the yellow metal.

Extremely weak economic data in the US and around the world, which suggests the economy will operate significantly below potential for a

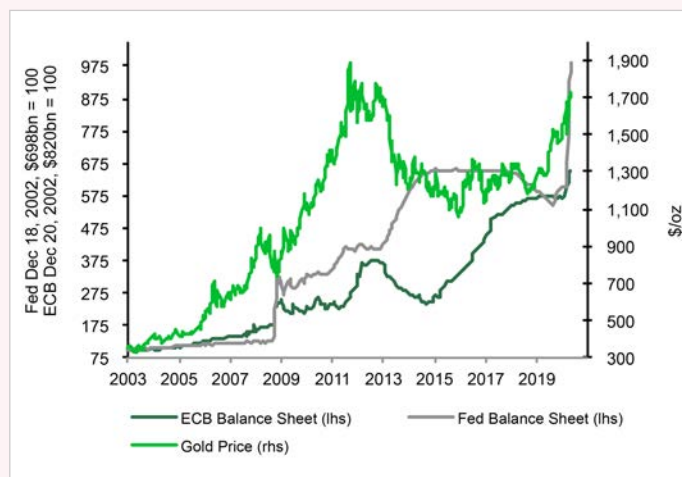


Figure 1 : Fed policy drives gold via real rates



Source: TD Securities, Bloomberg

Figure 2 : Expanding central bank balance sheets and gold so happy together



Source: Bloomberg, TD Securities

prolonged period, and all the disinflationary pressures this represents, also prompted some investors to be less enthusiastic about gold in the near-term. Real rates, which are a very powerful gold driver, may move higher given the Fed's steadfast commitment to keep policy rates at the zero bound but firmly above negative territory, at least for now.

Continued squaring of Comex positioning, which is driving strong flow of physical gold into North America, pressuring futures against physical gold, and generating liquidity stresses after the recent exchange for physical (EFP) blowout, along with the lack of physical demand in India, China and a move into risk assets such as equities as they post unexpectedly strong performance, have all reduced investor interest. The total gold exchange activity, which fell 56% m/m to 18 kilotonnes in April 2020, with Comex volumes dropping from 32 kilotonnes in March to just 13 kilotonnes in April, along with higher implied volatility is a case in point demonstrating less appetite from trader.

The upward creep in real interest rates, risk appetite and physical market dynamics will likely prevent another 20% jump, as we saw after the initial coronavirus driven collapse. Indeed, this along with a strong presence of commodity trading advisors (CTAs) and other algorithmic traders and limited risk capital (credit) availability for prop trading by institutional funds, suggest that gold is likely to remain range-bound with a strong risk of gravitating to the lower bound for the next quarter or so.

To demonstrate this point, even statements by Bank of England governor Andrew Bailey not ruling out negative rates and the recent drift of Fed Fund futures into negative territory were not enough to precipitate a lasting breakout to the upside.

#### DOMESTIC PRESSURES, ACCOMMODATING CENTRAL BANKS, GEOPOLITICS, LESS GLOBALIZATION LONGER-TERM UPSIDE CATALYSTS

After a period of stagnation during which prices may hover in the lower bound of the recent trading range near \$1,700/oz, the yellow metal should see resurgence in investor interest and move back on a path towards \$2,000+/oz. This level is very near the inflation-adjusted high reached in September 2009, which was the last time the market expected central banks to keep monetary accommodation in place as the economy started to follow a path to recovery.

Assuming the funding stresses moderate and there is an orderly post Covid-19 normalisation of the economy, without any major setback that would necessitate another series of shutdowns, disinflationary pressures should start to abate and with that the appetite for gold should recover. It is very likely that the post Covid-19 world will be very different than it was just a few months ago. It will be one where

**IT IS VERY LIKELY THAT THE POST COVID-19 WORLD WILL BE VERY DIFFERENT THAN IT WAS JUST A FEW MONTHS AGO. IT WILL BE ONE WHERE THE ECONOMY IS FUNCTIONING AT BELOW POTENTIAL, WITH HIGH LONG-TERM UNEMPLOYMENT AND WITH GOVERNMENTS WHO WILL WANT TO SOLVE THESE PROBLEMS BY SPENDING TRILLIONS OF DOLLARS, WHICH THEY DO NOT HAVE.**

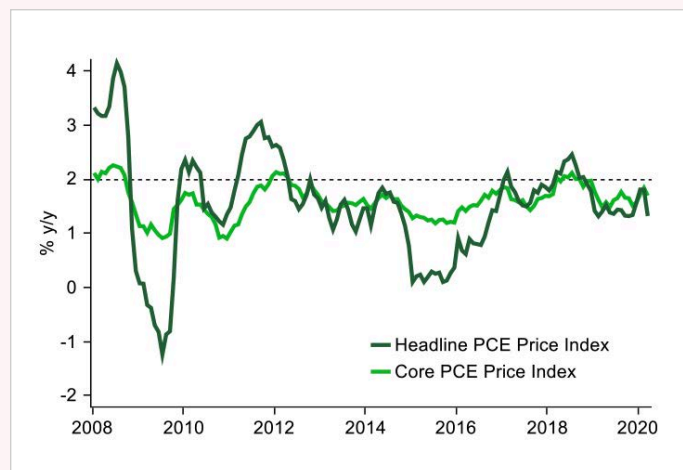
the economy is functioning at below potential, with high long-term unemployment and with governments who will want to solve these problems by spending trillions of dollars, which they do not have.

Conversely, central banks will provide virtually unlimited liquidity and will have the willingness to buy up a significant portion of public, private and corporate debt. In their quest to bring the economy to full employment, governments will continue to deficit spend, and central banks will very likely allow inflation to move above their current targets of 2%. There will also be a risk of de-facto monetisation, should deleveraging become a threat.

Policy rates are expected to remain at zero, even as inflation expectations move higher, and with that there will be a considerable number of investors who will try to protect their wealth against a stealth currency debasement. It is a well-established fact that over the very long-term, gold has outperformed fiat currencies.

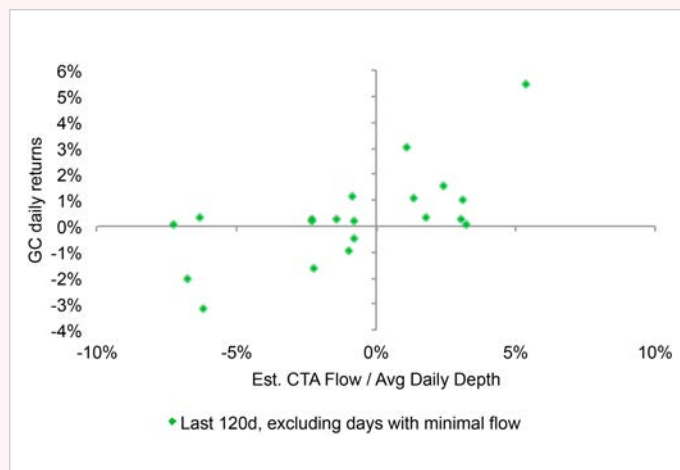
This post Covid-19 world will very likely turn out to be structurally different, with globalisation being reversed. This implies that critical and strategic supply chains will be brought closer to home for security of supply, as well as for strategic and employment reasons. This likely means higher costs due to the loss of efficiency and the use of higher cost domestic labour in the developed world. This would be a negative supply shock of sorts, which the Fed and other western central banks would no doubt accommodate. As such, above target inflation would be possible even if the economy is functioning below potential – a form of stagflation.

**Figure 3 : Economic weakness suppressing inflation, lifting real rates — keeping gold in the lower bound of the range for now**



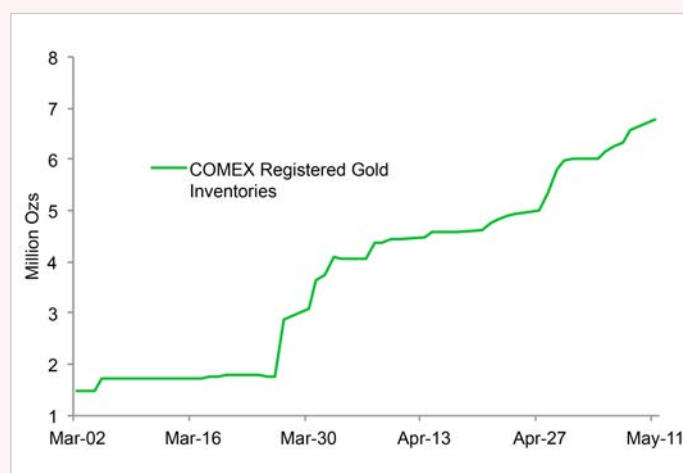
Source: BEA, TD Securities

**Figure 4 : Liquidity takers exacerbate intraday momentum amid shallow markets**



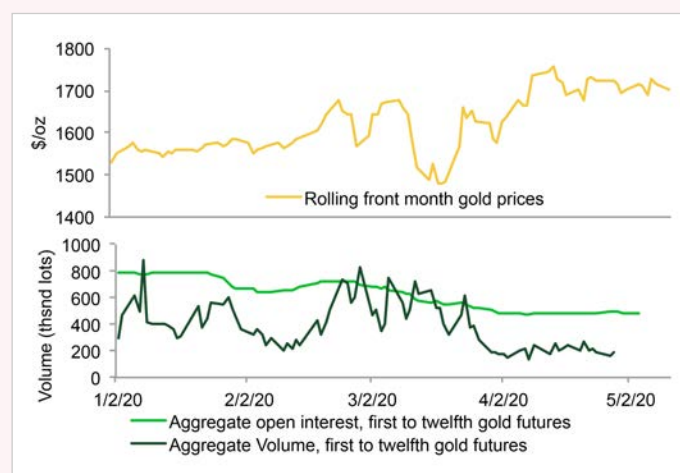
Source: Bloomberg, TDS Commodity Strategy

**Figure 5 : Ample amounts of gold in registered inventories**



Source: Bloomberg, TDS Commodity Strategy

**Figure 6 : Open interest continues to wane amid low volume despite bullish narrative**



Source: Bloomberg, TDS Commodity Strategy

### LOW REAL RATES, CURRENCY DEBASEMENT CONCERNS AND SKYROCKETING DEBT POSITIVES LONGER-TERM UPSIDE CATALYSTS

Once the post Covid-19 economic trajectory is well defined and health issues are managed with some certainty, the economy should have a good base to start a sustained recovery, albeit a prolonged one given the massive dislocation and insolvencies faced by small business and individuals. Negative real interest rates will likely be the order of the day for a long time, which make gold relatively cheap and desirable to hold in absolute and relative terms.

And, since it is no one's liability, which is quite opposite to the government paper that will be issued to support all the spending needed by the trillions to fund the various stability programs throughout the G7, gold has a clear path towards \$2,000+/oz.

**THERE IS STRONG EVIDENCE THAT GOLD PERFORMS WELL WHEN DEBT IS SKYROCKETING. AND, DEBT IS AT A RECORD HIGH, WITH A VERY HIGH PROBABILITY IT WILL REACH MUCH HIGHER LEVELS.**

There is strong evidence that gold performs well when debt is skyrocketing. And, debt is at a record high, with a very high probability it will reach much higher levels. We can only hope it does not go out of control, forcing aggressive monetisation.

To avoid sudden deleveraging, rates must be kept low and liquidity high, including central bank purchases (or quasi-monetisation). Thus far and in the post great recession central bank interventions, inflation only manifested in financial assets, but it did not move into the sphere of real goods and services as was feared – likely due to the cyclical components but also due to structural components such as globalisation, demographics and technology.

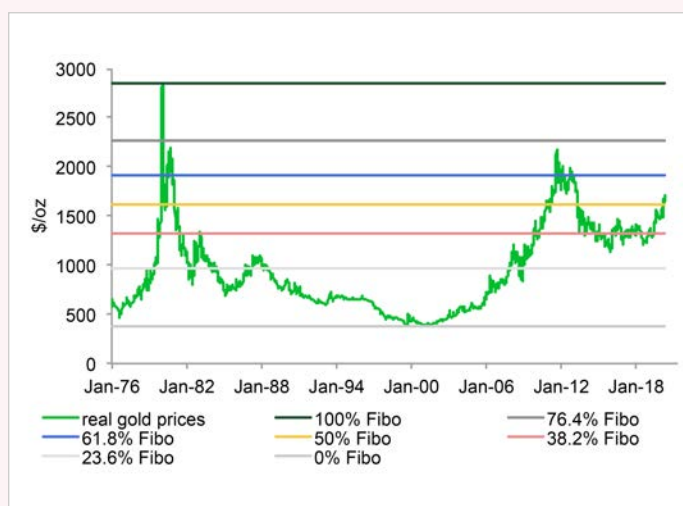
### DEBT A MANA FOR THE YELLOW HEDGE

With the coronavirus fiscal response in full swing, the global debt burden is set to rise dramatically in 2020; gross government debt issuance soared to a record high of over \$2.1 trillion in April, more than double the 2017–19 average of \$0.9 trillion.

As social distancing and sheltering-in-place became the norm across most mature economies, the current global recession will begin with \$87 trillion more in global debt than at the onset of the 2008 financial crisis driven slowdown. Based on Institute of International Finance (IIF) data, using a simple top-down projection, if net government borrowing doubles from last year's levels – and there is a 3% nominal global economic contraction (which could be significantly worse) –

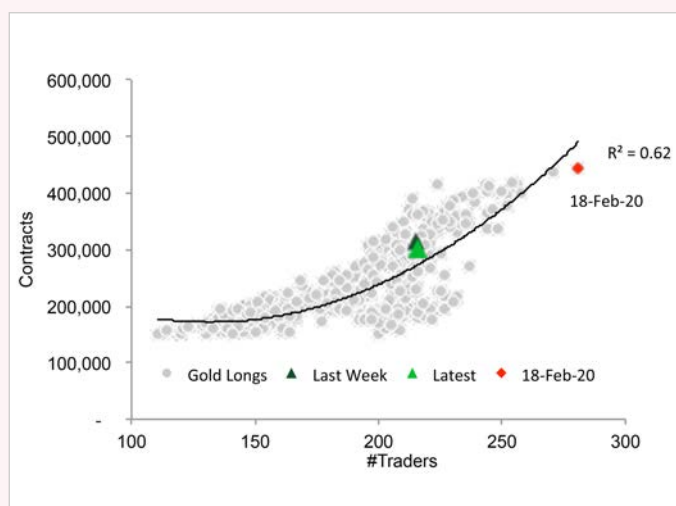


Figure 7 : Gold targeting historic high longer-term



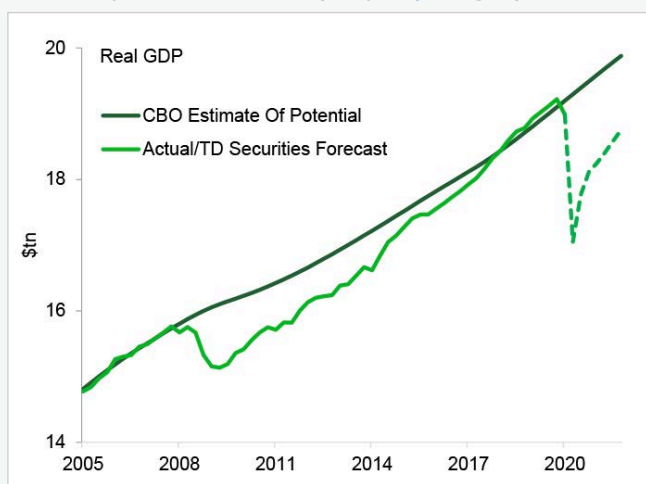
Source: TD Securities, Bloomberg

Figure 8 : A bullish outlook with no bulls in sight



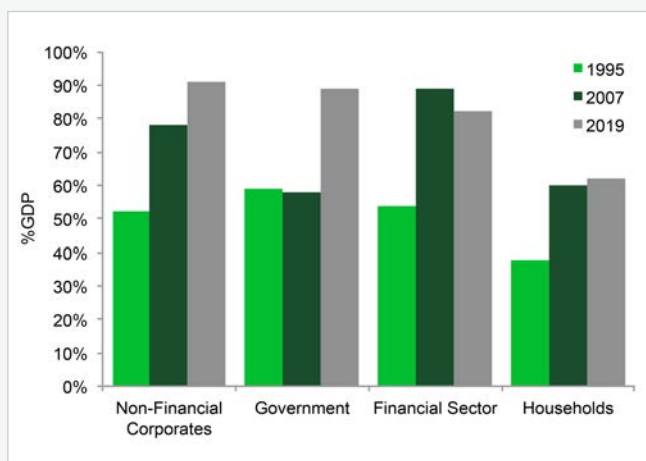
Source: CFTC, Bloomberg, TDS Commodity Strategy

Figure 9 : Outsized net decline in GDP implies lots of slack and a very accommodative Fed policy for prolonged period



Source: BEA, CBO, TD Securities

Figure 10 : Covid-19 to see world's debt surge to 342% in 2020



Source: TD Securities, IFI

the world's debt is set to surge from 322% (\$255 trillion) of GDP to over 342% (\$263 trillion) this year.

To stimulate employment, it is likely that the Fed and other key central banks will keep rates low for longer and will no doubt be very pragmatic in how they respond to an inflationary drift higher in order to avoid a deleveraging. Given the massive amount of global debt, markets will worry about monetisation and purchasing power debasement via the use of negative rates for a prolonged period. Considering it has been a challenge to hit inflation targets for so long, it's almost a given that central bankers will not worry if core inflation moves above the 2% target touted by most central banks in some form for a while.

The current price range near \$1,700/oz or a sell-off in the near-term should be considered temporary, with the previously discussed bullish macro factors eventually set to take charge. Further, the fact that some 6 million oz of annualised mining gold production is shutdown due to Covid-19 measures and lingering logistical issues making physical shipments extremely hard, will likely serve as additional catalysts moving the price toward \$1,900/oz before the yellow metal reaches escape velocity toward a \$2,000+ handle next year.



**BART MELEK** has over 20 years of experience analysing precious/base metals, energy, and financial markets, as well as North American and global economies. He has worked closely with commodity, equity and FX trading desks in Toronto, New York, Chicago, London and Singapore, and has numerous forecasting distinctions and top global rankings to his credit. Bart contributes to the TD Securities strategic view and

is a commentator for leading media organizations. Previous to joining TD, Bart was a global commodity strategist and senior economist at another major global financial institution.



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