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YEARS

# GFMS GOLD SURVEY 2017 Q3 Update & Outlook



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## GLOBAL REVIEW AND OUTLOOK

- *In September gold prices rose to their highest level for thirteen months due to an escalation in rhetoric and actions on the Korean Peninsula that had a considerable impact on the price at the time and impacted consumption.*
- *Gold prices over \$1,300 meant that physical demand slipped compared to the prior quarter, and while up 7% year-on-year, this lacklustre level of demand is still some 22% lower than two years earlier and key to the burgeoning surplus.*

The gold market's attention in the third quarter of 2017 has been centred on four developments. First the introduction of LMEprecious on 10th July which has got off to a solid if arguably unspectacular start. Second, the impact of the Goods and Service Tax in India and third, the announcement that the Fed would start unwinding QE and the increased likelihood of a rate rise in December. Fourth, the fiery rhetoric and actions emanating from President Trump and President Kim Jong-un were key to gold rocketing to \$1,351 per oz. However, it is noticeable that subsequent comments about "rocket man" and "dotard" did not prevent prices descending. This correction was unsurprising in our view as the price had moved too far and too fast, a view that was underpinned by physical demand in major Asian and middle Eastern markets drying up at these price levels and western investor demand remained modest. Furthermore, while the price peak on 8th September coincided with the Chinese agreeing to tighten sanctions, much of the subsequent developments have been rhetorical flourishes between the United States and Korea and have been viewed sceptically by some as to whether they make military action any more likely.

Taking Q3 2017 as a whole, while it is true that physical demand was 7% higher year-on-year this is effectively damning with faint praise. Physical demand was at its lowest level for a year, indeed if we strip out the exceptional situation in 2016 it marked the lowest quarterly total since Q4 2009. Given that was coupled with only modest ETF purchases this led to the largest surplus at the net balance level since Q4 2005 (when prices averaged just \$483).

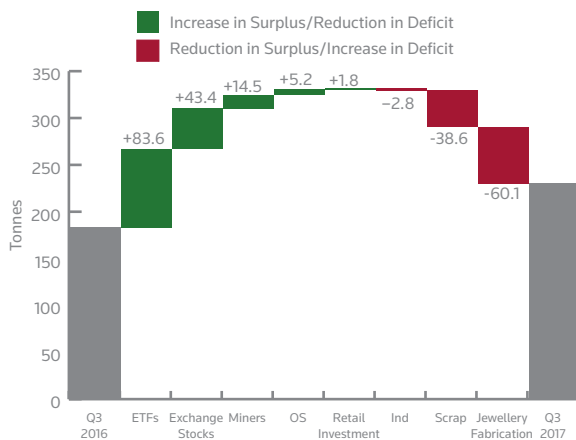
### WORLD GOLD SUPPLY AND DEMAND

(tonnes)	Q3 2015	Q4 2015	Q1 2016	Q2 2016	Q3 2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017	YoY %
<b>Supply</b>										
Mine production	852	820	757	794	844	837	756	797	841	-0.4%
Scrap	282	293	346	321	347	289	330	311	308	-11%
Net Hedging Supply	20	19	57	21	-10	-36	-17	-5	8	n/a
<b>Total Supply</b>	<b>1,154</b>	<b>1,131</b>	<b>1,160</b>	<b>1,136</b>	<b>1,181</b>	<b>1,091</b>	<b>1,068</b>	<b>1,103</b>	<b>1,157</b>	<b>-2%</b>
<b>Demand</b>										
Jewellery Consumption	565	639	424	406	427	600	453	499	475	11%
Jewellery Fabrication*	599	618	449	436	467	540	533	534	527	13%
Industrial Fabrication	91	88	86	89	89	91	92	92	92	3%
...of which Electronics	64	61	61	64	63	66	67	67	66	4%
...of which Dental & Medical	8	8	7	7	8	7	7	7	8	-3%
...of which Other Industrial	19	19	17	17	18	18	18	18	18	2%
Net Official Sector	152	120	47	37	76	98	49	85	71	-7%
Retail Investment	308	319	245	233	212	349	267	231	210	-1%
...of which Bars	221	244	192	173	164	255	207	174	157	-5%
...of which Coins	86	75	53	60	48	94	60	58	54	12%
<b>Physical Demand</b>	<b>1,149</b>	<b>1,146</b>	<b>827</b>	<b>795</b>	<b>844</b>	<b>1,078</b>	<b>941</b>	<b>942</b>	<b>900</b>	<b>7%</b>
<b>Physical Surplus/Deficit</b>	<b>4</b>	<b>-14</b>	<b>333</b>	<b>341</b>	<b>337</b>	<b>13</b>	<b>128</b>	<b>161</b>	<b>257</b>	<b>-24%</b>
ETF Inventory Build	-60	-69	336	233	114	-158	109	36	30	-73%
Exchange Inventory Build	-39	-15	15	76	40	-45	-5	-13	-4	n/a
<b>Net Balance</b>	<b>103</b>	<b>70</b>	<b>-18</b>	<b>32</b>	<b>183</b>	<b>216</b>	<b>24</b>	<b>138</b>	<b>230</b>	<b>26%</b>
<b>Gold Price (London PM, US\$/oz)</b>	<b>1,124.3</b>	<b>1,106.5</b>	<b>1,182.6</b>	<b>1,259.6</b>	<b>1,334.8</b>	<b>1,221.6</b>	<b>1,219.5</b>	<b>1,256.6</b>	<b>1,277.9</b>	<b>-4%</b>

Source: GFMS, Thomson Reuters \*Jewellery Fabrication is used in the collation of the Physical Surplus / Deficit and Net Balance

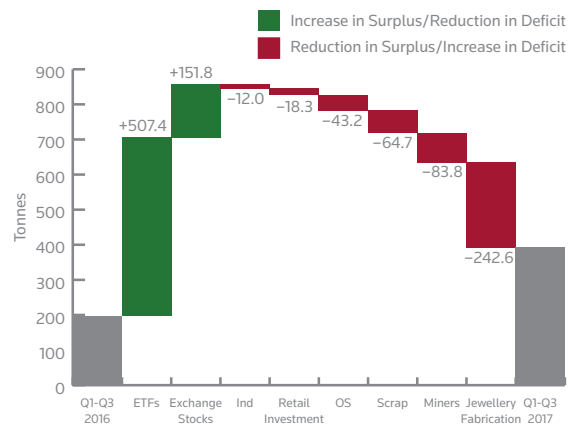
Totals may not add due to independent rounding. Net producer hedging is the change in the physical market impact of mining companies' gold loans, forwards and options positions.

Q3 2017 BALANCE COMPARED TO Q3 2016



Source: GFMS, Thomson Reuters \* Sum of production and hedging.

Q1-Q3 2017 BALANCE COMPARED TO Q1-Q3 2016



Source: GFMS, Thomson Reuters \* Sum of production and hedging.

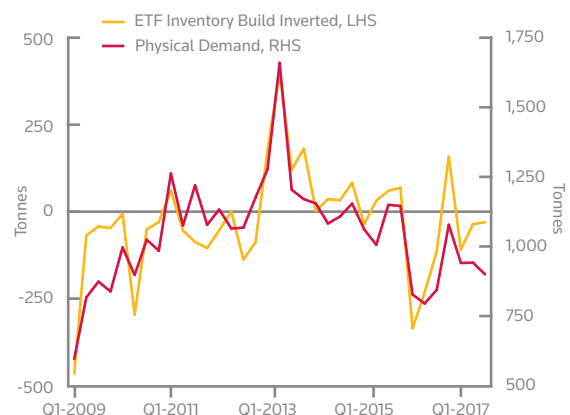
Looking at the largest consumers indicates why global demand is still anaemic, with Chinese jewellery demand still falling on a year to date basis, despite a recovery in the third quarter. However, given the improvement in the economy there this is arguably a disappointing result as retailers focus on higher margin products that generally require less gold. Meanwhile in India gold demand in Q3 2017 increased by 16% year-on-year to 167 tonnes, but this was the lowest in four quarters. In fact jewellery fabrication increased by 30% year-on-year last quarter contrary to expectations that fabrication demand would slow after the imposition of the Goods & Services Tax (GST). That said, the gains are attributed to the lower base last year. Comparing to more than 100% gains noted in Q1 and Q2, fabrication tapered as a large part of stocking was done ahead of the GST implementation.

Whether it is just the third quarter or looking at the first nine months as a whole it is noticeable in the charts above that the improvement in physical demand has not been enough to offset the slowdown in ETF purchases from the stellar surge last year. The latter has been hindered by weakness in the key U.S. market and net redemptions in China. Retail investment has been similarly unspectacular although at least coin demand has been better than the difficult summer months with Chinese and U.S. coin demand being the key drags again. Meanwhile supply has stuttered this year despite mine production being resilient as Indian scrap flows dropped by two thirds.

OUTLOOK

**Gold prices hit the buffers in recent weeks, as the relative softness in physical demand in Asia coupled with lacklustre investment demand from western economies has unsurprisingly resulted in prices dropping back below \$1,300 per oz. However, we think this is a healthy correction for the price that had become overextended and think it has formed a base for a more sustainable move above \$1,300 later this year and to rise still further in 2018 as it averages \$1,360 and hits a 2018 peak of almost \$1,450. Crucial to this is the growing risk inherent in key global equity markets, with the S&P 500, DAX and FTSE all recording all time highs in recent weeks. Even if this doesn't lead to a marked correction we believe the growing risk will spur some investors to make (or increase) their allocation in gold rather than being caught too heavily in an equity fuelled basket. This is likely to be supported by continued geopolitical tensions, whether from events in Korea, Catalunya or even the upcoming Italian election or Brexit negotiations. Further details and accompanying one and three year forecasts for gold prices and supply & demand components are available on Thomson Reuters Eikon.**

QUARTERLY PHYSICAL DEMAND & INVERTED ETF BUILD



Source: GFMS, Thomson Reuters

# CHINA

- Demand for gold from the domestic jewellery market was resilient as the Chinese economy and spending sentiment improved. Indeed, fabrication volumes actually increased 11.5% on an annual basis in the third quarter, the first annual growth recorded in the third quarter since 2013. Having said that, total fabrication volume still fell 1.5% year-on-year in the first three quarters of this year.
- Despite the revival of the jewellery sector in the third quarter, we estimate that Chinese gold demand still fell on an annual basis in the first three quarters this year, dragged down by a fall in retail investment. The largest casualty was the coin sector, dropping by over 65% year-on-year in the first three quarters, to just 7.7 tonnes.

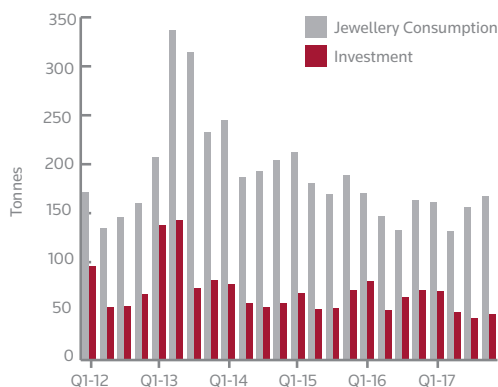
In the first three quarters of the year, Chinese gold demand from the jewellery fabricators totalled 458.9 tonnes, compared to 466.1 tonnes in the corresponding period last year, a modest fall after several years of double-digit percentage declines. While this positive trend is encouraging, we think the short term recovery is due to a revival in the level of spending in an improving economy, but the fundamentals of the industry remain – that retailers are focusing on selling high margin products that in general would require less gold (i.e. 18-carat, gem sets etc.) as opposed to the model that used to focus on quantity selling in the past. For example, fabrication volume in the non pure gold segment continued to grow strongly, recording an over 20% annual growth in the first three quarters. Sales of Three-Dimensional (3D) hard gold, a technique that uses pure gold to make large pieces but actually hollow inside and thus very light weight, have been very strong. Therefore, with the continual emergence of these new product mixes taking market share from the traditionally pure gold segment, we expect Chinese gold demand from this sector to continue to fall in the medium to longer term.

Despite the revival of the jewellery sector in the third quarter, we estimate that Chinese gold demand still fell during the quarter on an annual basis, mostly dragged down by a fall in retail investments. The largest casualty was the coin sector, dropping by over 65% year-on-year in the first three quarters, to just 7.7 tonnes. Bar investment also fell, by 11.7%, to 152.7 tonnes, due to a lack of faith in the gold price. Indeed, when the international gold price breached the \$1,300/oz level towards the end of August, more Chinese took profits at that level than chasing the market higher.

Gold holdings in the Chinese ETFs have seen significant redemptions this year and as of the end of September contained just 24 tonnes, compared to 36 tonnes as of end December 2016.

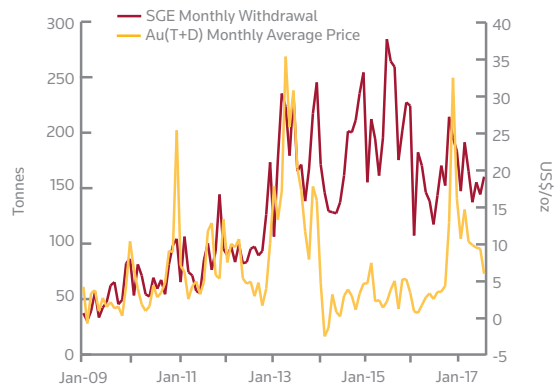
Total gold demand totalled 221.5 tonnes in the third quarter, a 0.4% year-on-year decline from the corresponding period last year. In the first three quarters of this year, total Chinese gold demand amounted to an estimated 671.8 tonnes, a 5.2% retreat on an annual basis.

## CHINA JEWELLERY CONSUMPTION & RETAIL INVESTMENT



Source: GFMS, Thomson Reuters

## SGE WITHDRAWALS



Source: GFMS, Thomson Reuters

Chinese gold imports from Hong Kong and Switzerland, which typically contribute over 85% of total imports in any month, totalled just 47.3 tonnes in August, a 47.9% month-on-month decrease and 29.4% decline on an annual basis. The soft import data in August also dragged down China's gold imports from these two major hubs to a total of 691.0 tonnes in the first eight months this year, compared to 723.2 tonnes in the corresponding period last year, representing a 4.5% decline. To put the data into context, cumulative imports from these two markets increased by 2% on an annual basis for the first half of the year.

Some analysts track China's gold import data arguing that this is a clear gauge of the country's gold market and demand trends. However, the gold import data is not a good proxy for the country's true demand, because the import decisions made by banks are more than just for satisfying market demand. For example, whenever the Chinese gold premia are at high levels, banks are inclined to import more gold for the arbitrage opportunity, even if the end demand is not there. Other than the supply and demand fundamentals, the strength of the yuan also plays a critical role influencing the Chinese premia. In addition, the volume of gold an individual bank can import in a year relies on a quota system – banks need to submit an annual forecast on how much gold they intend to import for the full year, and then be approved by the People's Bank of China (PBOC) at the beginning of each year. Therefore how much gold banks choose to import every year depends on how much they want to maintain their import quotas on a yearly basis and not necessarily on the needs of end users. As a result, even if gold consumption falls, or even if the Chinese gold price actually falls into a discount to the international benchmark, Chinese gold imports volume will not be falling at a rate that will truly reflect the decline in the true demand, simply because banks want to at least maintain their import quotas year after year.

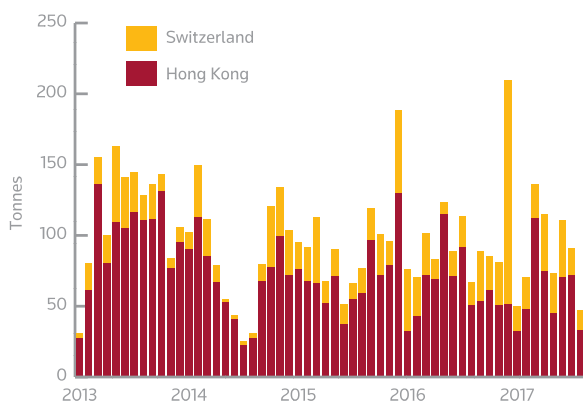
A final impact that can further muddy the waters when looking at bullion flows is the amount of gold that is being smuggled out of China. As was the case last year gold bars and scrap are being smuggled out of China to other locations in significant volumes, particularly to Hong Kong. The main reasons for these flows are most likely to avoid paying taxes, to reallocate assets outside China and to obtain greater access to the U.S. dollar. Last year this figure would have exceeded 100 tonnes with flows close to this if not higher in 2017.

A final touch on a rumour that China is going to introduce a yuan-denominated oil futures contract that is freely convertible to gold. The feedback we have had confirmed from industry participants is that the yuan-denominated oil futures should be available for trading before the end of this year, but that gold convertibility feature is too complicated to implement from their view, and debunk it as total nonsense.

## CHINA MARKET OUTLOOK

**Looking forward, we expect gold import data in September to be certainly improved compared to August, as jewellery fabricators will have started to stock up inventories anticipating the one-week long Labour holiday in October. However, import volumes may turn to the weak side in October and November, especially considering that some of the smaller Chinese banks have already used up their annual import quotas in September. While it is possible that**

### GOLD IMPORTS FROM HONG KONG & SWITZERLAND



Source: GFMS, Thomson Reuters

**the PBOC may grant extra quotas to these banks in December to import more gold in the last month of the year, most of the industry participants view this an unlikely scenario. Another important factor deciding the trend in the Chinese gold premia will be the strength of the yuan. Normally the weaker the yuan against the dollar, the higher the Chinese gold premia will be. The yuan has depreciated against the dollar in the fourth quarter three years in a row since 2014, and this year could possibly be the fourth consecutive year, given that there is a high probability that the Federal Reserve will raise interest rates in December. For the full year, we expect China's consumption of physical gold could record a modest decline compared to last year.**



## QUARTERLY JEWELLERY CONSUMPTION

(tonnes)	Q3 2015	Q4 2015	Q1 2016	Q2 2016	Q3 2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017	YoY % change
<b>Europe</b>										
Turkey	14.4	11.2	9.7	10.9	10.1	9.0	8.8	10.3	11.1	10%
Russian Federation	8.0	8.6	7.5	7.3	7.1	8.3	7.4	8.3	8.7	22%
United Kingdom	4.3	15.7	3.8	3.7	4.4	13.3	3.0	2.8	3.8	-14%
Italy	2.5	9.3	2.5	3.5	2.4	9.2	2.4	3.4	2.3	-4%
Spain	1.8	2.6	1.5	1.8	1.7	2.5	1.5	1.8	1.7	2%
France	1.6	6.0	2.4	2.1	1.5	5.8	2.3	2.0	1.5	1%
Germany	1.3	5.8	1.6	1.8	1.3	5.7	1.6	1.8	1.3	3%
<b>Europe Total</b>	<b>33.8</b>	<b>59.2</b>	<b>28.9</b>	<b>31.1</b>	<b>28.4</b>	<b>53.7</b>	<b>26.9</b>	<b>30.6</b>	<b>30.4</b>	<b>7%</b>
<b>North America</b>										
United States	36.5	58.9	18.8	32.0	32.2	55.4	21.9	29.8	34.7	8%
Canada	4.1	5.8	3.3	4.3	3.8	4.9	3.2	4.6	5.0	32%
Mexico	1.4	1.6	2.1	1.9	1.7	1.6	2.1	1.9	1.6	-1%
<b>North America Total</b>	<b>42.0</b>	<b>66.3</b>	<b>24.2</b>	<b>38.1</b>	<b>37.6</b>	<b>61.9</b>	<b>27.2</b>	<b>36.3</b>	<b>41.3</b>	<b>10%</b>
<b>Asia</b>										
China	169.2	188.7	170.2	146.4	132.5	163.4	160.3	129.2	153.4	16%
India	181.0	186.7	72.9	74.2	120.4	195.5	109.6	183.4	140.9	17%
Iran	9.8	9.3	9.0	9.6	10.6	10.6	11.5	11.1	11.5	9%
Saudi Arabia	13.5	12.6	9.1	10.7	9.0	9.3	8.5	10.1	8.9	-1%
UAE	11.2	12.1	16.8	10.5	7.6	11.3	15.8	11.1	7.4	-3%
Indonesia	9.7	11.6	10.0	6.5	7.2	10.5	11.1	9.1	7.3	1%
South Korea	7.2	7.1	7.3	6.2	6.5	6.9	6.7	5.9	6.1	-6%
Bangladesh	3.8	4.9	4.9	3.8	4.1	5.3	5.3	4.9	5.4	32%
Kuwait	6.3	5.5	5.1	5.0	5.1	5.0	5.2	4.6	5.4	6%
Israel	6.2	6.2	4.8	5.0	5.3	5.1	4.7	4.9	4.8	-10%
Japan	5.0	4.6	5.7	4.6	4.8	4.7	5.2	4.4	4.8	-2%
Iraq	4.8	4.6	3.6	3.3	3.7	3.8	3.3	3.1	3.3	-11%
Vietnam	3.1	3.1	5.3	4.6	3.0	3.4	5.1	4.7	3.2	9%
Jordan	4.8	3.7	3.1	3.6	3.5	3.7	2.9	3.4	3.2	-9%
Pakistan	5.1	6.8	2.1	3.8	3.2	5.1	3.8	4.2	3.1	-3%
Thailand	4.0	4.1	4.6	4.0	3.1	3.2	5.5	4.8	3.0	-3%
Lebanon	4.9	4.1	2.6	2.9	2.7	3.0	2.5	2.6	2.4	-9%
Malaysia	2.6	2.4	1.3	1.2	2.1	2.3	1.1	1.3	2.0	-5%
Singapore	1.8	3.0	2.2	2.6	1.9	2.7	1.9	2.3	1.9	0%
Bahrain	2.6	2.5	2.1	1.7	1.9	2.1	2.0	1.8	1.7	-9%
Sri Lanka	0.4	0.3	0.8	0.7	0.8	1.4	1.9	1.8	1.2	50%
Other Asia	5.9	6.9	5.6	5.6	4.6	6.6	5.4	4.9	4.8	5%
<b>Asia Total</b>	<b>472.3</b>	<b>498.9</b>	<b>355.0</b>	<b>322.8</b>	<b>349.7</b>	<b>472.8</b>	<b>385.3</b>	<b>419.2</b>	<b>392.1</b>	<b>12%</b>
<b>Africa Total</b>	<b>11.6</b>	<b>9.1</b>	<b>8.7</b>	<b>6.4</b>	<b>6.5</b>	<b>6.3</b>	<b>6.7</b>	<b>5.4</b>	<b>5.4</b>	<b>-16%</b>
<b>South America</b>										
Brazil	2.2	2.1	4.0	4.7	2.0	2.2	4.1	4.6	3.1	53%
Other South America	3.0	3.1	2.9	3.1	3.0	2.9	3.0	3.0	3.0	0%
<b>South America Total</b>	<b>5.2</b>	<b>5.2</b>	<b>6.9</b>	<b>7.8</b>	<b>5.0</b>	<b>5.1</b>	<b>7.1</b>	<b>7.6</b>	<b>6.1</b>	<b>22%</b>
<b>World Total</b>	<b>564.9</b>	<b>638.7</b>	<b>423.7</b>	<b>406.1</b>	<b>427.2</b>	<b>599.8</b>	<b>453.2</b>	<b>499.1</b>	<b>475.2</b>	<b>11%</b>

Source: GFMS, Thomson Reuters

sBEad\*coin



extraterrestrial



# INDIA

- **Indian gold demand in Q3 2017 increased by 16% year-on-year to 167 tonnes, however this was the lowest in four quarters.**
- **India imported 105 tonnes of gold in Q3 2017; up 31% year-on-year.**
- **Jewellery consumption was higher by 17% year-on-year at 141 tonnes; it was still the lowest since Q4 2016 and 5% lower than the average quarterly demand this decade.**
- **Investment demand increased 10% year-on-year in Q3; however it was 62% lower than the average quarterly demand this decade.**

Official bullion trade has slowed significantly on challenges related to the Integrated Goods and Services Tax (GST) payment at the time of imports. Further, the additional duty benefit to refiners in excise free zones has reduced to zero post GST and as a result the number of active refiners has halved to just ten. Demand in Q3 was not supported by strong official imports, and supplies largely emerged from unofficial sources and the import of gold at concessional duty from South Korea (estimated at 27 tonnes). Our estimate is that unofficial trade increased by 80% year-on-year in Q3 to 46 tonnes. It may be counter-intuitive to think of an increase when GST was supposed to bring traceability but the cost of compliance has increased the cost of gold. In India the majority of retailers are still small-sized standalone and family-run businesses, and a large number of them do not fret to walk the less compliant path to protect their customers' interest and to avoid being taxed.

## BARTERING OFFICIAL WITH UNOFFICIAL

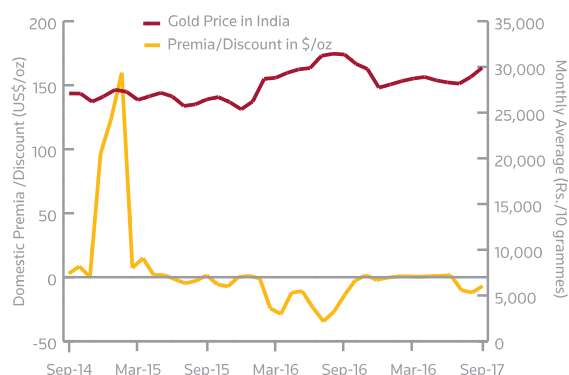
Example: A retailer makes a jewellery sale against cash to its customer. The customer bill would account only for the making charge and the GST, that too wherever the retailer finds it necessary. This is possible by showing every sale by the retailer being for the exchange of old jewellery for new. The cash collected against the sale is used to purchase unofficially imported gold and these are then matched with the sale of jewellery for jewellery. The retailer would then re-melt these bars in the backyard to show it as melted scrap jewellery and this is then resent to manufacture 22-carat jewellery. Thus, in the books this would show that the retailer did make a sale and collected GST from the customer, but the replenishment is that of unofficially sourced gold. This was primarily in jewellery of ticket size less than Rs. 200,000/- where customer ID proof is not mandatory. As this was happening, the government included the jewellery industry into the Prevention of Money Laundering Act (PMLA) whereby each business with turnover of over Rs. 200,00,000 had to supply additional reporting as per PMLA laws. Further to that it also meant that sales over Rs. 50,000 had to be supported with a ID proof of customer. As a result, the customers were reluctant to purchase, impacting businesses of medium and large scale retailers. And most business eventually moved to retailers who

INDIAN JEWELLERY CONSUMPTION & RETAIL INVESTMENT



Source: GFMS, Thomson Reuters

INDIAN GOLD PRICE



Source: GFMS, Thomson Reuters; NCDEX; MCX

followed a path that weren't in-principal to the trade, and these retailers constitute the most in numbers. Following various representations from the industry the circular was rescinded early October .

## JEWELLERY FABRICATION HOLDS FIRM

Jewellery fabrication increased by 30% year-on-year last quarter contrary to expectations that fabrication demand would slow after GST. That said, the gains are attributed to the lower base last year. Comparing to more than 100% gains noted in Q1 and Q2, fabrication tapered as a large part of stocking were done ahead of the GST implementation. At the Indian International Jewellery Show (IIJS) the rush to place orders was strong; this was in contrast to last year's show, where orders were just at average levels. The business dynamics are however going through a transition. Some of the major changes that we are noticing include, for instance, retailers now seeing an increase in their inventory turnover ratio, indicating that there is an increase in sales. More specifically this ratio had started showing an improvement since late last year. That said, amongst the organised segment there has been a consistent rise in inventory since 2012 to 2016 and a large part of the rise was attributed to the wedding segment, as this has been a key differentiator over generic products. This segment is seen to score well while others excluding the fast moving categories should see more rationalisation of inventory. It is observed that the number of days in inventory has increased over last five years from an average 140 to 220 particularly with retailers who have been expanding the stores across the country.

## GOVERNMENT GETS TOUGH ON ROUND TRIPPING

A circular in August 2017 made it mandatory that exports of any gold jewellery, articles or medallions cannot be more than 22-carat and exporters were not allowed to take gold on loan aside from domestic banks. These two measures were primarily introduced to clamp down on round tripping. Following this, medallions exports volumes dropped sharply in Q3 2017 and so did the total round tripping volumes by approximately 70%. That said, the additional cost to export in the form of 22-carat jewellery is only 0.15%, so it will not be a surprise to see volumes resume, but they would be likely to be less than 80 tonnes a year, that is less than half of the annual average this decade.

## INDIAN MARKET OUTLOOK

The recent publication by the Reserve Bank of India highlighted that 11% of the wealth held by Indian households is in gold. It is less likely that this number could see a significant shift in the recent future with the changing demographics which supports a stronger demand. Also demand from agricultural households is estimated to increase by 21% in the 2017-18 crop year as per our econometric model studying the relation between monsoon and gold demand. This likely to have a positive impact on the unofficial trade given that most of the transactions are likely to be in cash.

### INDIAN GOLD IMPORT ESTIMATES BY SOURCE PRODUCT

Imports (tonnes)	Q2 2016	Q3 2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017
<b>Banks</b>						
Duty paid	26.9	20.8	81.6	83.6	87.1	31.7
Duty free	5.7	9.3	13.9	12.0	11.4	12.9
<b>Nominated agencies</b>						
Duty paid	10.9	5.3	5.3	34.3	48.4	12.7
Duty free	25.8	33.1	37.5	39.6	48.1	15.2
<b>Fine gold from doré</b>	14.1	9.4	65.3	51.1	68.3	31.3
<b>Direct import by exporters</b>	2.5	2	1.3	1.2	1.4	1.5
<b>Total</b>	<b>77.9</b>	<b>79.9</b>	<b>233.9</b>	<b>236.1</b>	<b>271.9</b>	<b>105.3</b>
<b>Net import</b>	<b>44</b>	<b>35.6</b>	<b>181.2</b>	<b>183.1</b>	<b>163.8</b>	<b>75.7</b>
<b>Unofficial Imports</b>	53.5	25.2	23.3	15.6	22.8	46
<b>Average price (Rs/10 grammes)*</b>	<b>29,652</b>	<b>31,285</b>	<b>29,090</b>	<b>29,056</b>	<b>28,902</b>	<b>28,989</b>
<b>Average premia/(discount) in domestic in \$/ounce **</b>	(15.6)	(25.1)	(1)	0.3	0.8	(7)

Source: GFMS, Thomson Reuters; IBJA\*, NCDEX\*\*, Various Sources

## OFFICIAL SECTOR

- ***In the first three quarters of 2017 net central bank purchases rebounded to post a gain of 27% year-on-year, at 204 tonnes despite the absence of Chinese buying. Crucially there was less selling and Turkish buying supported the traditional high level of acquisitions from Russia and to a lesser extent Kazakhstan.***

Last year saw the lowest level of net central bank purchases since 2010 at 258 tonnes, down 42% year-on-year. Even as that was happening we cautioned repeatedly that we were of the view that this was not the start of a change from the strong central bank buying that has prevailed throughout this decade, but was instead a fluctuation. The first half of 2016 was the crucial period for the softer tone overall last year, due in no small part to sales by the Venezuelan central bank at that time, and hence the year on-year comparisons show a sharp upturn so far in 2017. What has been slightly surprising is the composition of some of this activity; there are two, somewhat offsetting, factors in this regard.

One that is widely publicised and commented on is that the PBOC has not reported making any purchases of gold since October last year, having previously announced acquisitions for 17 months in a row. Some commentators have argued that this is due to the fact that this followed the inclusion of the renminbi into the SDR basket in October 2016, which was widely seen as a key driver in the opening up of the gold reserve data prior to the IMF making a decision on 30th November 2015 to include the renminbi. However, we believe that it is more likely that the key driver behind the PBOC stopping purchases was their falling U.S. dollar reserves, albeit from the exceptional - and unprecedented - level of almost 4 trillion dollars in June 2014. As they approached reserves to 3 trillion.

One central bank that has picked up the slack however in recent months has been the Turkish central bank. The Turkish central bank made purchases of 6.8 tonnes in May and a further 13.5 tonnes in June, which was its first acquisitions of gold this century (note: this is separate from the change in commercial banks' holdings at the central bank). This has continued with further acquisitions of 8.0 tonnes in July and 8.9 tonnes in August (data for September is yet to be available at the time of writing). Meanwhile Russia remains the largest purchaser. In the first half of 2017 the Russian central bank acquired 100.6 tonnes. While on an individual monthly basis their level of buying varied considerably this pace of acquisition is broadly consistent with them having bought 206.4 tonnes in 2015 and 200.7 tonnes in 2016.

There was only one other country that sold and another that bought substantial amounts of gold in the first half of 2017. Kazakhstan continued its six-year strategy of regular purchases and as a result added 21 tonnes, a slightly faster pace than the 16 tonnes bought in the same period of 2016. Meanwhile on the sales side, Azerbaijan sold the remaining 20 tonnes of its holdings.

On 23rd August the Bundesbank announced that it had completed the transfer of its gold transfer process. This was three years ahead of its 2020 target and means it now has no gold stored in Paris and more than half of its reserves stored domestically, in Frankfurt.

## OUTLOOK

***Russia is set to be the largest reported purchaser for the 6th successive year in 2017. Indeed by the end of this calendar year its holdings are likely to be around 1,825 tonnes, as it strengthens its position as the 6th largest holder globally. Intriguingly, this means that if China continues the recent trend of not changing its reported holdings then the gap between the two will have narrowed to around 17 tonnes. To put that in context there have been many months in recent years when Russia has acquired that in one month so we could be just three/four months away from Russia overtaking China and moving into the top five global gold holders.***

***That said, foreign exchange reserves are rising again, albeit not dramatically, and it seems likely to us that sooner rather than later the PBOC will resume making purchases. This will help to underpin the pace of global gold purchases which on a net basis we expect to be around 150 tonnes in the second half of 2017.***

## UNITED STATES

- **Retail investment fell 55% to 6.0 tonnes this past quarter. This double-digit decline was mainly driven by a drop in U.S. Mint sales in the period, exacerbated by a decline in small bar demand.**
- **Jewellery consumption increased by 8% from last year to total 34.9 tonnes in Q3. Domestic production nudged slightly lower whilst net imports of jewellery increased at a healthy pace.**

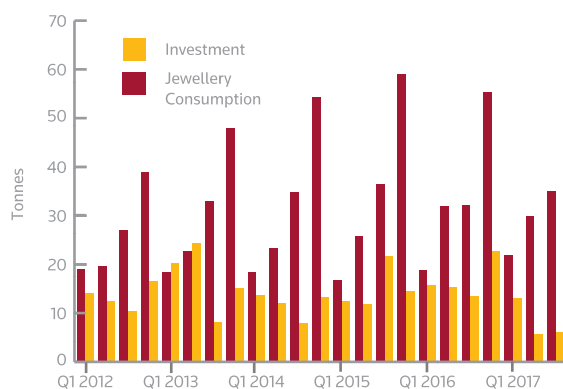
This year, U.S. Mint sales have been a smidgeon of the sales volumes recorded in the last year. As such, the U.S. Mint recorded its third consecutive quarterly decline in coin sales with the third quarter 76% below that recorded in the third quarter of the prior year. U.S. Mint sales represent gold coin demand at the wholesale level but anecdotal evidence suggest its a good proxy for retail demand too, at least in regards to the sales of newly minted coins. Since the Mint does not sell used coins, newly minted coin sales do not describe the total picture of the underlying bullion coin market. Net new demand from coins has been strongly in decline, but transactions conducted on the secondary market still seem robust. Premia of backdated bullion coins and bars have fallen to unprecedented lows, with some recording a spread of merely 50bps earlier in the year. That seems to have recovered to as much as 200-250bps in the third quarter this year.

Market participants recorded heavy re-sale of coins with investors exiting the precious metals market altogether. The appetite for stocks and other risk-prone assets seems to be far more prevalent than the need to hedge yourself against currency debasement or macro-economic shocks. Net-bar hoarding in Q3 fell by approximately 30% in the United States to 4.3 tonnes. On the institutional side trading has slowed as well this year. There seems to be business sporadically but transactions are far and few between.

Demand for gold to produce jewellery fell 2% in Q3 from last year while gold contained in jewellery purchased by consumers rose 8%. Lower gold prices in July benefited gold jewellery demand in the period, as these price movements coincided with seasonal upticks in demand ahead of the wedding and graduation season that usually starts in June. Continued annual increases in disposable incomes also benefited demand growth. Cumulative consumer expenditure on jewellery increased by 4% from a year ago, according to Bureau of Economic Analysis data.

Gold demand from other sectors rose 1% year-on-year, driven primarily by higher electronics usage. Semi-conductor sales increased 11% in North America year-to-date whilst prices for printed circuit boards have fallen considerably over the past years. Year-to-date up to August indicated a rise in the book-to-bill ratio, which indicates that demand is ahead of supply. The continued electrification of products increases the amount of circuit boards that are being used globally. Gold content per circuit board is declining but the amount of circuit boards in circulation is still rising annually in North America.

### U.S. RETAIL INVESTMENT & JEWELLERY CONSUMPTION



Source: GFMS, Thomson Reuters

### UNITED STATES MARKET OUTLOOK

**Jewellery demand growth is expected to continue to flourish in the final quarter of this year. Although the industry is facing challenging times in terms of reaching its customers and with substitution pressures from within and outside the jewellery sector, consumer spending to date has been good and we expect that to remain the case in the final quarter of the year. Retail investment, on the other hand, is expected to remain weak. For the U.S. Mint, contrary to last year when sales were very strong, this year seems to be a writeoff. Bar demand is also expected to remain sluggish, with investors more interested to invest in other asset classes, unless tensions with North Korea increase.**

## QUARTERLY RETAIL INVESTMENT

(tonnes)	Q3 2015	Q4 2015	Q1 2016	Q2 2016	Q3 2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017	YoY % change
<b>Europe</b>										
Germany	27.6	26.5	23.0	23.7	20.4	37.3	28.1	19.7	20.8	2%
Turkey	8.7	4.6	5.4	4.2	5.2	11.7	8.0	17.7	12.0	131%
Switzerland	11.3	9.9	12.0	9.7	8.1	11.5	12.4	8.0	7.4	-8%
Austria	9.2	8.1	5.5	4.2	2.8	8.5	3.7	2.7	4.8	70%
United Kingdom	4.4	6.1	5.3	5.5	3.2	5.3	4.9	5.6	3.1	-3%
Belgium	6.1	5.4	2.8	5.8	2.8	5.9	3.0	4.5	2.6	-5%
Netherlands	1.7	1.9	1.0	1.0	1.0	1.9	1.1	0.9	1.0	-2%
Spain	0.8	1.1	0.9	0.9	0.9	1.0	0.9	0.8	0.8	-5%
Luxembourg	1.7	1.6	1.3	1.4	0.7	1.8	1.4	1.3	0.7	-3%
Czech Republic	0.8	0.9	1.2	1.1	0.7	1.0	1.1	1.0	0.7	-3%
Poland	0.9	0.8	0.9	1.0	0.8	0.9	0.9	1.0	0.7	-10%
Other	3.6	4.8	3.8	3.4	3.2	5.1	3.1	2.9	2.5	-21%
<b>Europe Total</b>	<b>76.8</b>	<b>71.6</b>	<b>63.1</b>	<b>62.1</b>	<b>50.0</b>	<b>91.8</b>	<b>68.6</b>	<b>66.0</b>	<b>57.3</b>	<b>16%</b>
<b>North America</b>										
United States	21.6	14.4	15.8	15.3	13.4	22.6	13.0	5.5	6.0	-55%
Canada	11.0	9.2	7.1	7.1	6.1	11.9	12.0	3.9	4.0	-34%
Mexico	0.4	0.3	0.4	0.2	0.4	0.1	0.5	0.3	0.4	16%
<b>North America Total</b>	<b>33.1</b>	<b>24.0</b>	<b>23.2</b>	<b>22.7</b>	<b>19.9</b>	<b>34.5</b>	<b>25.5</b>	<b>9.7</b>	<b>10.5</b>	<b>-47%</b>
<b>Asia</b>										
China	53.1	71.5	80.3	50.9	63.9	71.4	70.2	43.7	46.5	-27%
India	54.8	55.5	7.1	29.6	22.0	74.7	29.6	38.7	24.3	10%
Thailand	14.0	22.3	13.5	12.3	12.1	17.1	19.5	17.0	21.0	73%
Vietnam	10.5	10.5	9.5	11.1	9.5	12.2	10.3	10.7	9.8	3%
South Korea	5.2	5.1	3.9	3.6	3.8	4.3	4.4	4.2	4.2	11%
Indonesia	2.0	3.1	3.8	3.8	3.5	3.6	3.7	3.5	3.3	-6%
Iran	11.9	11.5	4.9	0.9	-2.1	-1.2	3.5	3.3	2.7	n/a
Pakistan	4.2	3.8	1.8	3.1	1.8	3.8	2.1	3.2	2.1	17%
Saudi Arabia	3.7	3.7	3.4	2.7	2.5	2.6	2.8	2.2	2.0	-20%
UAE	2.8	2.6	1.4	1.9	1.8	2.9	1.5	1.7	1.9	6%
Taiwan	0.9	1.2	1.7	1.6	1.5	1.5	1.6	1.5	1.5	-3%
Singapore	1.7	1.9	1.8	1.5	1.5	1.7	1.9	1.6	1.5	-3%
Kuwait	1.4	1.5	1.1	1.1	1.1	1.3	1.2	1.1	1.3	18%
Malaysia	0.9	1.3	1.1	1.3	1.2	1.3	1.2	1.7	1.3	8%
Hong Kong	0.6	0.7	0.7	0.6	0.6	0.5	0.7	0.5	0.5	5%
Cambodia	0.6	0.7	0.6	0.6	0.5	0.6	0.6	0.6	0.5	6%
Sri Lanka	0.1	0.1	0.4	0.1	0.2	0.3	0.2	0.2	0.3	30%
Japan	8.3	6.3	2.6	4.6	2.0	3.0	-2.4	0.8	-3.6	n/a
Other Asia	3.2	3.1	2.7	2.6	2.4	3.3	2.8	2.7	2.4	0%
<b>Asia Total</b>	<b>179.8</b>	<b>206.2</b>	<b>141.5</b>	<b>133.7</b>	<b>129.7</b>	<b>204.6</b>	<b>155.1</b>	<b>138.7</b>	<b>123.2</b>	<b>-5%</b>
<b>Oceania Total</b>	<b>6.7</b>	<b>7.7</b>	<b>7.1</b>	<b>5.8</b>	<b>5.0</b>	<b>7.9</b>	<b>6.1</b>	<b>4.6</b>	<b>5.5</b>	<b>9%</b>
<b>Africa</b>										
S. Africa	8.6	7.7	7.9	7.8	6.8	12.7	10.5	11.2	12.7	88%
Egypt	2.3	1.6	1.4	0.7	0.8	-2.5	0.9	0.6	0.6	-25%
<b>Africa Total</b>	<b>10.9</b>	<b>9.3</b>	<b>9.3</b>	<b>8.5</b>	<b>7.5</b>	<b>10.1</b>	<b>11.4</b>	<b>11.8</b>	<b>13.3</b>	<b>76%</b>
<b>South America Total</b>	<b>0.6</b>	<b>0.6</b>	<b>0.6</b>	<b>0.6</b>	<b>0.6</b>	<b>0.6</b>	<b>0.6</b>	<b>0.6</b>	<b>0.6</b>	<b>0%</b>
<b>World Total</b>	<b>307.9</b>	<b>319.4</b>	<b>245.1</b>	<b>233.3</b>	<b>212.2</b>	<b>349.5</b>	<b>267.2</b>	<b>231.4</b>	<b>210.4</b>	<b>-1%</b>

Source: GFMS, Thomson Reuters

## MINE SUPPLY

- *Global mine production rose by two tonnes or 0.1% year-on-year in the first half of 2017. The largest increases were posted in North America and Africa, which rose by a combined 4% with the United States and Ghana leading the change. Asia and South America fell by 22 tonnes due to environmental concerns in China and severe weather conditions in Australia and Peru.*
- *Average Total Cash Costs rose by 6% in H1 2017 to \$665/oz, while average All-In-Sustaining-Costs (AISC) rose 5% year-on-year to \$874/oz. Capital expenditure is estimated to have jumped by 30% to \$6.1 Bn.*
- *The global producer hedge book contracted by 5 t on a delta-adjusted basis, in line with our expectations. Overall, 44 companies saw net decreases in their hedge position, while 15 companies increased the size of their hedge book.*

## MINE PRODUCTION

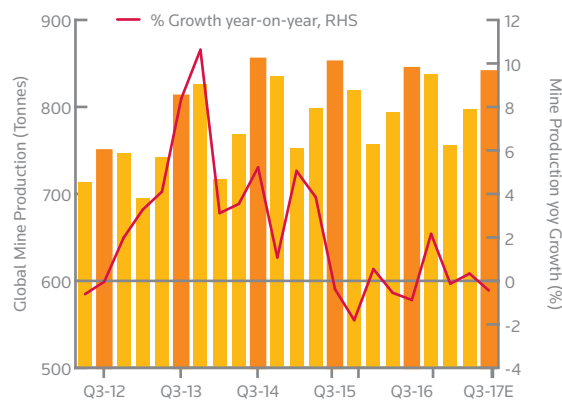
Global mine supply in the first half of 2017 reached a total of 1,552 tonnes, two tonnes above the same period last year. This marked a 1.5% compound annual growth rate (CAGR), down from 2.6% in H1 2016. Much of the gain came from the United States and Ghana, together with the resumption of concentrate exports from Grasberg in April. Further gains were noted in Suriname, where Newmont’s Merian operation ramped-up production to seven tonnes in the first six months to offset losses from mature operations in the region. Heavy rains in Peru stemming from an abnormal El Niño accelerated losses with artisanal and illegal mine production most affected. A similar impact was noted in Australia, where severe weather conditions led to losses at Telfer and Tanami.

Higher supply from the United States during H1 was led by strong output at Cripple Creek & Victor and Barrick Nevada, which managed to lift the country balance by an estimated 13 tonnes, or 12%, to 120 tonnes. Although we’ve noted a significant increase from other smaller public-listed companies, we maintain our view that there remains scope for an even stronger increase stemming from privately owned operations in the Midwest and West regions of the country.

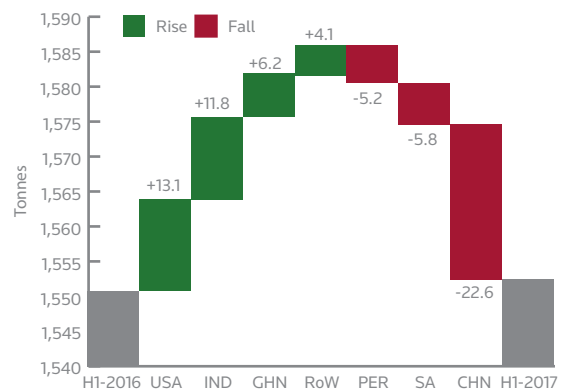
Chinese mine production registered the largest drop globally to total 207 tonnes in H1 2017, down 23 tonnes, or 9.8% year-on-year. While gold production in the second quarter did improve by a modest 4.1% compared to the first quarter this year, this was largely due to the production halts during the Chinese New Year holidays in the first quarter. The most important aspect that has dragged down China’s gold production so far this year is the government’s escalating efforts to fight pollution and increase attention to environmental protection. As a result, output from the country’s nonferrous smelters fell by 30% or 14 tonnes in tandem with a 2% drop in ‘mine-produced gold’ to total 65 tonnes.

Based on limited updated quarterly production reports and annual production guidance, we expect mine production to contract year-on-year in Q3 2017. We expect losses in China to accelerate as capacity is curtailed further. Industry consensus points to a considerable drop in Chinese mine production for the year as a whole.

### GLOBAL GOLD PRODUCTION



### YEAR-ON-YEAR VARIANCE





## PRODUCER COSTS

Total Cash Costs (TCCs) net of by-product credits rose year-on-year in H1 2017 from \$630/oz to \$665/oz led by higher unit cost inflation and lower grades in South Africa. Higher production costs were also posted across other countries, particularly in Australia, where TCCs rose due to production disruptions in the first quarter of 2017. As a result, the global dollar gross margin contracted by 3% to \$573/oz as higher crude oil prices (+26%) and stronger domestic currencies placed additional pressure on costs. Year-on-year, capital expenditure is estimated to have risen by 30% to \$6.1 Bn led by strong growth in expansionary capex. In tandem with this net change, the average All-In-Sustaining-Cost (AISC) posted another quarterly net increase, rising by \$43/oz to \$874/oz.

In South Africa producers continued to struggle to control costs, the highly labour intensive nature of the South African industry and union strength once again being a major cost driver. This led to wages increasing above the inflation rate which, coupled with a stronger rand (+14%) and lower output, caused TCCs to rise by 30% year-on-year to \$1,033/oz. Costs at South Africa's largest producing mine, the Kloof Driefontein Complex, rose by 27% to \$913/oz, while at Bambanani, TCCs surged by 48% to \$1,162/oz due to lower grades.

Australian cost inflation hit 3% year-on-year with costs rising to \$674/oz. A large proportion of this was due to the 3% appreciation of the Australian dollar against the U.S. dollar, while the integration of mining assets led to a partial offset. Heavy rainfall and a cyclone particularly affected operations in the Western Australia and Queensland, responsible for over three-quarters of the country's production. A similar impact was noted in Peru, where El Niño adversely impacted open pit operations like Yanacocha.

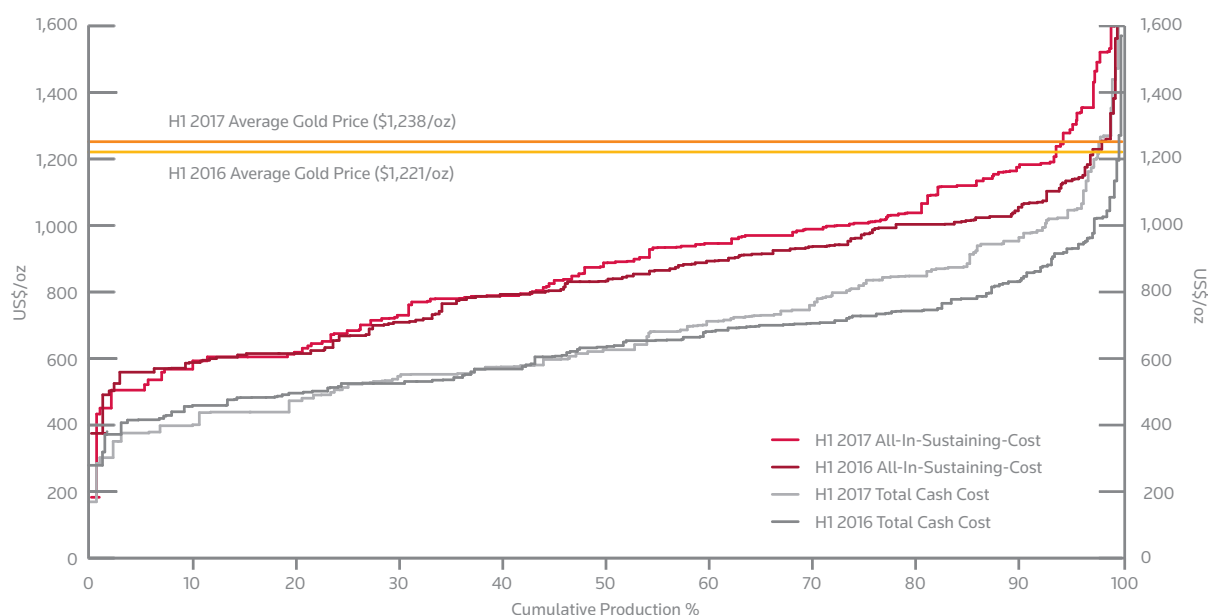
Going forward we expect costs to continue trending higher on the back of a sustained recovery in oil/energy costs and the depletion of higher grade resources.

### COST OF PRODUCTION AND GRADES

(US\$/oz)		H1 2016	H1 2017
<b>North America</b>	Total cash costs	608	612
	All-in Sustaining costs	816	847
	Processed grade, g/t	1.61	1.64
<b>South America</b>	Total cash costs	556	611
	All-in Sustaining costs	743	817
	Processed grade, g/t	1.89	2.12
<b>Australia</b>	Total cash costs	653	674
	All-in Sustaining costs	834	865
	Processed grade, g/t	1.59	1.58
<b>South Africa</b>	Total cash costs	793	1033
	All-in Sustaining costs	960	1186
	Processed grade, g/t	1.80	1.69
<b>Other</b>	Total cash costs	615	613
	All-in Sustaining costs	775	768
	Processed grade, g/t	1.9	1.86
<b>World</b>	Total cash costs	630	665
	All-in Sustaining costs	831	874
	Processed grade, g/t	1.76	1.78

Source: GFMS, Thomson Reuters

### WORLD TOTAL CASH AND ALL-IN SUSTAINING COST CURVES



Source: Company Reports; GFMS, Thomson Reuters

**PRODUCER HEDGING**

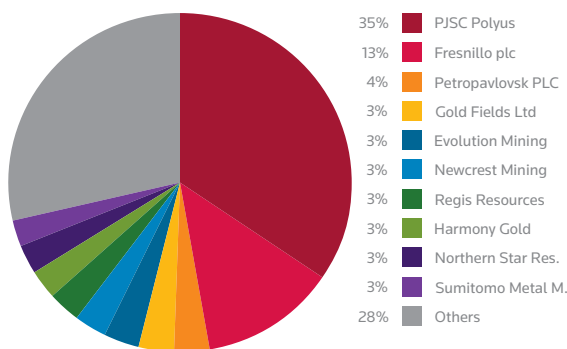
The global producer hedge book contracted by 5 t on a delta-adjusted basis during the second quarter of 2017, representing a 2% decrease on the hedge book total at the end of Q1 2017. As a result, the hedge book stood at a total of 229 t at the end-June. Over the second quarter, Australian based operators accounted for 23% of the gross de-hedging, with the majority of the net de-hedging coming from Evolution Mining (1.9 t), followed by Independence Group (0.6 t). The largest hedge was entered by Gold Fields, which covered 8.4 t of production for delivery over the next two quarters using a combination of collars and forward sale contracts.

Overall, 44 companies saw net decreases in their hedge position, while 15 companies increased the size of their hedge book. Of the net de-hedgers, PJSC Polyus saw the largest hedge book reduction as the company exercised 6.6 t of barrier options, followed by Petropavlovsk and Fresnillo plc with a combined 5.3 tonnes.

Australian-based companies accounted for 23% of the second quarter's gross de-hedging, down from 35% in the previous quarter, with a total of 16 companies delivering into forward sales or collar structures, while nine others were net hedgers. Gold Fields, Citigold, and Silver Lake Resources were amongst the largest net hedgers in Australia.

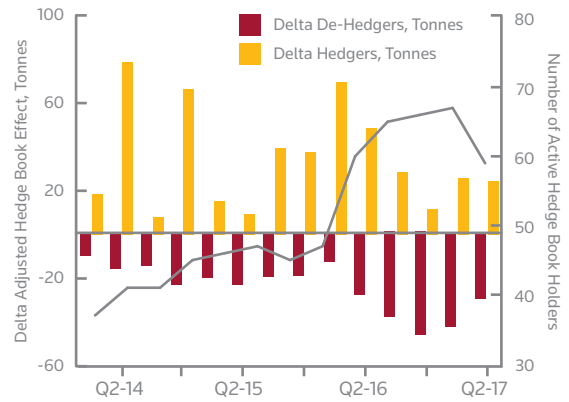
Following modest hedging in H1 2016 led by Australian producers, the second quarter of 2017 marked the fourth consecutive quarter of net de-hedging in the global hedge book. With the weighted time to maturity of vanilla options trending lower since end-2014, further gains were capped as the scheduled unwinding of existing hedge contracts accelerated. However, we expect producers to turn to net-hedging in the third quarter as evidenced by the string of company announcements following the break above US\$1,300/oz in late August. Weak physical demand, particularly in Asian markets, shed light on what was labelled as an unsustainable price move driven by geo-political tensions. This led producers like Yamana Gold, Acacia Mining, Teranga Gold and Sumitomo Metal Mining to hedge a combined 14.7 tonnes using a combination of collars and forward sale contracts. For the third quarter as a whole, we expect the hedge book balance to grow by an estimated eight tonnes on the back on new project financing deals and a much due realignment in the option book balance following a spike in 3-month risk reversals.

**CORPORATE HEDGE BOOKS (BY # OF CONTRACTS)**



Source: GFMS, Thomson Reuters

**ACTIVE HEDGE BOOK HOLDERS**



Source: GFMS, Thomson Reuters

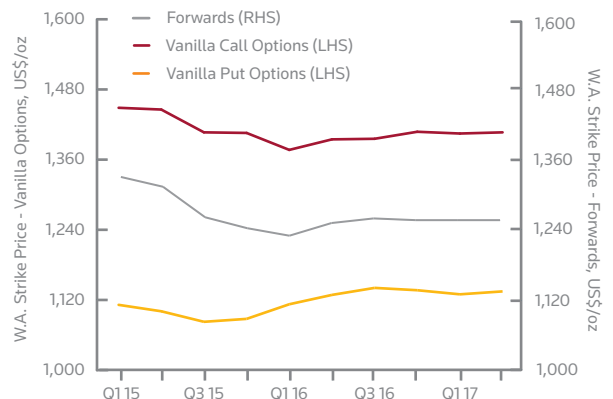
**COMPOSITION OF THE DELTA-ADJUSTED HEDGE BOOK**

(tonnes, end-period)

	Q2-16	Q3-16	Q4-16	Q1-17	Q2-17	QoQ
Forward Sales	178	181	164	168	169	+1%
Options	119	106	87	67	60	-10%
Total	297	287	252	235	229	-2%

Source: GFMS, Thomson Reuters

**HISTORICAL WEIGHTED AVERAGE STRIKE PRICES**



Source: GFMS, Thomson Reuters

## INDUSTRIAL DEMAND

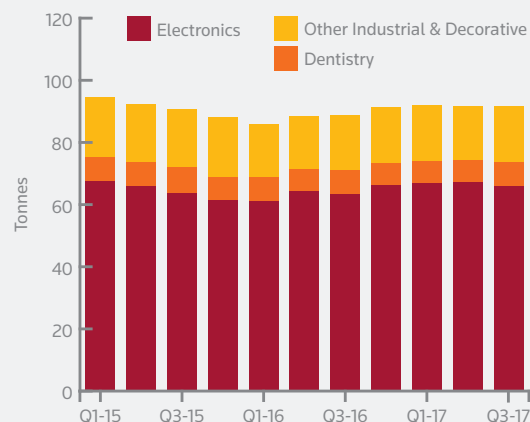
Gold demand for industrial and dental applications continued the recovery phase that developed in the final quarter of last year to record another year-on-year increase in Q3 17, this time of just over 3%. The gain lifted offtake year to date to 275.3 tonnes, 5% stronger than the corresponding period last year. Much of the increase in demand was driven by growth in offtake from the electronics sector that was boosted by a combination of inventory restocking and higher consumer demand. Elsewhere, other industrial and decorative fabrication also recovered lost ground, gaining 2% on the back of improved performances from the Asian region, while gold used in dental applications continued the long term decline in the second quarter, retreating 3% from the corresponding period in 2016.

The electronics sector has continued to rebound strongly after emerging from a slump in recent years as a weaker global economy and ongoing substitution away from gold to cheaper alternatives drove demand lower. Demand growth in the third quarter, while modest at 3%, was the fourth quarterly rise in succession and perhaps an indication that this sector has turned the corner and would appear set for a return of sustained growth. Indeed, fine gold offtake recovered 5% or nearly 7 tonnes over the 2016 level for the first half of the year on the back of stronger demand for gold bonding wire and plating solutions such as potassium gold cyanide (PGC), but remains more than 25% below the peak seen prior to the Global Financial Crisis.

Strong demand and rising prices for memory integrated circuits (ICs) and other semiconductors has resulted in stronger-than-expected sales for the global semiconductor industry in 2017. According to the World Semiconductor Trade Statistics (WSTS) the global semiconductor market will increase 17% to \$394 billion this year. The growth rate for 2017 will be the highest that it's been since 2010 when sales increased more than 30%. Worldwide sales of semiconductors in August 2017 grew by an impressive 24% year-on-year to US\$35 billion. Industry experts suggest that the impressive growth this year is largely due to the overall strength of semiconductor demand and increasing prices, especially for dynamic random-access memory (DRAM) and NAND flash. As a result, memory prices and revenue have both increased. Robust demand from the smartphone segment and from the auto industry have lifted offtake for semiconductors. In the case of the latter, demand for enhanced safety features and more advanced electronics within the dash of the vehicle such as touch panels has contributed to the rise. Another industry segment that has aided electronic growth this year has been for light-emitting diodes (LED) demand which has continued to enjoy healthy expansion as a result of growth within both the automotive sector and residential markets. In addition, manufacturers of hybrid vehicles and electric vehicles have increasingly embraced new technologies. Turning briefly to individual regions, East Asia led the way, with a solid recovery in gold bonding wire production in South Korea accounting for a significant proportion of the rise. Elsewhere in Asia, demand from the other bonding wire manufacturing hubs such as Singapore, China, and Japan all recorded a rise in demand, with the latter was also buoyed by increased demand for gold targets and plating solutions.

Increased demand in Q3 17 from the other industrial and decorative segment was driven by an improving economic outlook, coupled with a greater level of price acceptance, with total offtake for the quarter rising 2% year-on-year to deliver a year to date increase of 3% over the corresponding period in 2016. Indian demand was broadly stable as growth for plating solutions and wires was met by a rise in imports, negating the need for an increase in local production. Elsewhere, demand in Europe was moderately weaker while in North America offtake within this segment was flat. East Asian demand was also stronger as demand for targets and plating solutions gathered momentum, led by Japan, South Korea and China. Finally, gold used in dental applications continued its secular downtrend, slipping 3% year-on-year to 7.6 tonnes for Q3.

### INDUSTRIAL DEMAND



Source: GFMS, Thomson Reuters

## GERMANY

- *German retail interest was lacklustre apart from a brief flurry of activity in July.*

The past decade has seen German retail investment being arguably not just the most important theme of German gold demand but that of overall European precious metal offtake. In this vein last year ended with a burst of demand and this trend continued throughout the traditionally quieter period of January and February before a slowdown emerged in March. The past six months or so though have seen retail investors taking something of a backseat in the industry, with the sole exception of July when there was a short lived but appreciable upturn in orders. This flurry of activity was encouraged by bargain hunters as the price briefly dropped back in euro terms below €1,100. However, this was not sustained as prices recovered and there were no indications of it returning when prices returned to this level. To be clear, German retail investment has been far from disastrous. Indeed with the stellar start to the year performance so far this year is broadly flat; it has just lacked recent impetus to return to former peaks. This subdued performance has not been helped by the DAX recording record highs and a relatively rangebound performance by gold in euro terms of late. Despite the ongoing coalition talks post the German election and the dramatic events in Catalonia it was crystal clear from discussions that neither had sparked any meaningful change in activity in Germany.

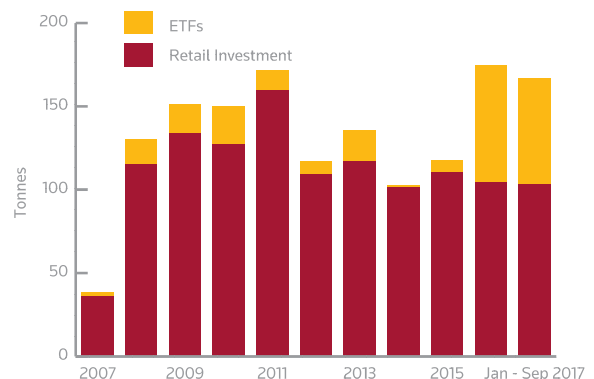
One trend is the growing importance in the German gold investment mix coming from ETF holdings. In the first nine months of 2017 ETF demand represented 38% of German gold investment compared to it being a mere 5% since the first German gold ETF was launched in 2007 and the end of 2015. There are a number of reasons that might be driving this shift. First, and in our view easily the most significant, is the significant upturn in institutional interest, from nascent levels, in the past two years. This has been helped by the turnaround in prices and a view that prices were “low” and hence the risk/reward was advantageous. In support of this thesis that it is due to institutional buying we would note the scale of much of the ETF buying on particular days - when more than 10 tonnes are bought. Second, the ETFs have now been around for a number of years and cautious investors may now be more comfortable with these products. Third, individuals, and especially millennials, are increasingly comfortable with electronic payments and hence the imperative for holding physical oneself is arguably receding for some.

Elsewhere the German market is generally seeing robust trends as the economy performs well and its exports focus is helped by the most synchronised upswing in global economic activity for many years. Silver industrial demand is performing especially well with strong growth in activity across all major sectors leading to growth overall approaching 8% year-to-date, even after accounting for continued thrifting. The picture is much more muted for gold industrial demand, but it still represented an improvement on the prior downtrend. In the gold jewellery market meanwhile demand is growing 3% overall with a shift away from 14ct to both 8ct and 18ct.

### GERMAN MARKET OUTLOOK

The German retail investment market is likely to improve in the coming weeks as it gains from seasonal gift purchases to a far greater extent than anywhere else in Europe. However, we also expect retail investment to be appreciably lower year-on-year than the stunning end to 2016 as prices slumped and Trump's election raised geopolitical fears. This underperformance is likely to be compounded by our expectation of a price rise in the remainder of 2017. Looking to 2018, we think German institutional buying is likely to strengthen further as the potential for a correction in German equity markets encourages a growing number of institutions to increase holdings to diversify their portfolios.

GERMAN INVESTMENT



Source: GFMS, Thomson Reuters

## TURKEY

- **Turkish gold imports are expected to post a new record this year driven by stimulus from the central Bank and strong jewellery and coin demand.**

Turkish gold imports rose a whopping 568% year-on-year to 290 tonnes over the January - September 2017 period with June (46.3 tonnes) and July (62.9 tonnes) reporting their strongest individual months on record. Considering the current strong pace of imports it is likely the total number at the end of the year will be a new record, surpassing the high of 302 tonnes recorded in 2013.

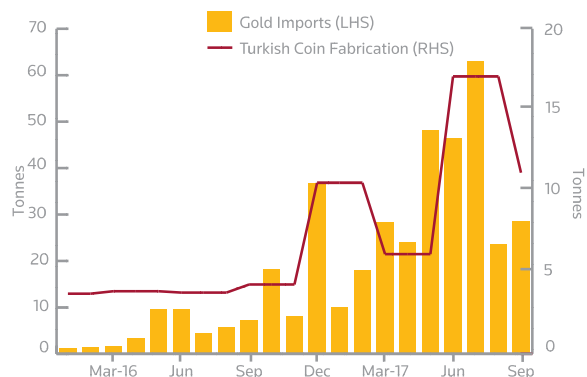
The strong rise in imports has been mainly a function of a pickup in jewellery manufacturing for the domestic as well as export markets and a rise in investment demand. We estimate that domestic jewellery fabrication rose 15% year-on-year to approximately 73 tonnes in Q1-Q3 2017. Most of this was driven by strong exports with precious metals in value rising 64% to approximately \$3.0 billion over the Q1-Q3 period this year. At \$2.7 billion, gold jewellery accounted for 92%, whereas the other 8% was made up of diamond containing gold jewellery, silver jewellery, scrap of precious metals, articles of pearls, precious and semi-precious stones and some other items. The main gold jewellery exports destinations were surrounding countries such as UAE (37%) and Iraq (28%) followed by the United States (6%) and Hong Kong (5%).

In volume terms, precious metals exports rose 76% to approximately 4,000 tonnes over January – September 2017. Exports of precious metals waste and scrap accounted for three quarters of the volume. The value of scrap is very low, containing only small amounts of fine metal. Precious metals scrap, polishing wastes and factory sweepings are usually refined in Turkey. However, Turkey does not have the technology to refine precious metals (mainly gold and silver) from the slurry that is left after the refining process. This material is shipped abroad for processing, chiefly to facilities in Belgium and Germany. The strong rise in exports of this sort of waste therefore supports the increase of activity at the Turkish refiners over the January – July 2017 period.

Strong jewellery manufacturing however was not the only part of the story; gold coin fabrication also surged in Q1-Q3 this year by 189% reaching 34 tonnes. Gold in Turkey is considered not only a store of value but also as an investment, a gifting item and as a means of payment. As such, the trading of gold coins exhibit a very lively primary as well as secondary market in Turkey. The state owned Turkish mint, Darphane, is the fifth largest gold coin fabricator globally behind the United States, South Africa, Canada and China, accounting for an 11% market share. The only difference from some of the other mints is, however, that the majority of the Darphane's coin fabrication is sold domestically, whereas the other major mints usually also have substantial exports.

Through the introduction of various bits of gold friendly legislation, the central bank of Turkey has been very active in recent years to try to stimulate the gold market. The first major gold friendly policy put in place was the introduction to hold gold as a reserve requirement by the commercial banks in 2011. The FX facility has been considerably utilised over the years leaving little spare capacity. The introduction of gold as a reserve requirement eased some of that pressure as is visible in more recent years. Second, banks will be able to free up more liquidity to provide lending, stimulating the economy in the process. Third, and more importantly, however, is the attempts of the central bank to get a portion of the “under-the-pillow” gold from retailers into the financial system. In addition to all the measures it has put in place for the first time since 1980s, the central bank also purchased 21 tonnes of gold itself in the second quarter of this year and 16.8 tonnes in the third (with September data yet to be released).

### TURKISH INVESTMENT & COIN FABRICATION



Source: GFMS, Thomson Reuters; UNITC



## Side by side with the technologies that usher in new eras

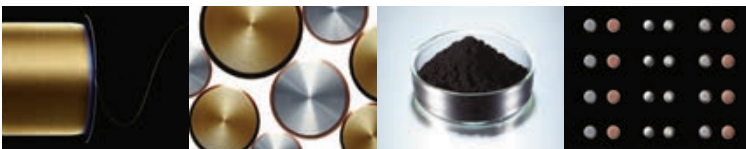
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## UK

- ***Shaky consumer confidence coupled with rising precious metal prices in dollar terms, and exacerbated by a sharply weaker sterling since the Brexit vote, have led to appreciably softer offtake from the UK jewellery sector. Our findings from the International Jewellery London (IJL) show that the industry is not taking it lying down.***

Against this backdrop UK hallmarking statistics remain dire, with the number of gold pieces down by 23% for the first nine months of the year compared to a year earlier. The picture for the other metals appears more mixed with silver up 13%, while platinum rose 1% and palladium down 5% for the aforementioned period. However, describing this as a mixed picture is putting a brave face on a real struggle for the sector. Platinum and palladium are more resilient as they are primarily used in wedding and engagement rings. The main reason we believe the picture is poorer than it appears is that the silver hallmarking statistics are unduly positive. A significant volume of branded pieces are being hallmarked by UK assay offices that had previously been moved to other countries; a key reason why we believed that consumption in the UK was stronger than the UK hallmarking figure suggested in prior years for silver.

Given this backdrop it was unsurprising that discussions with major industry players in September at the IJL show at Olympia, London (the biggest such annual event in the UK) talked of a challenging period. The picture was not entirely uniform though with watch demand stronger than for jewellery, while there are signs that the mid-top end of the market has been holding up better than the lower end. This is arguably because the portion of the price which is prone to the underlying precious metal price is lower in percentage terms. Hence the increase is less likely to have been passed on and when it has been would make a smaller difference to the amount sold. Our discussions with the trade support this theory as margins have been squeezed. Discussions at IJL however were far from uniformly downbeat and there were some signs that the past month to six weeks has been a touch better. Those who are significant sellers of earrings or chokers also highlighted that these areas have been very popular. What's more various companies are taking a number of initiatives that fall outside redesigns of the product offering from a fashion perspective and which may encourage demand (even if on some occasions this is not the sole driver behind the move). These often centre on the customer experience, ethics and emotional ties that influence the decision to purchase precious metal jewellery.

Four key examples are the Responsible Jewellery Council (RJC), Fair Luxury, Made in Britain, and Skin Kind. The RJC undertook a workshop to explore the benefits of membership, which has rapidly expanded in recent years. It explained how it is increasingly important to understand that a growing group of consumers, particularly millennials, are asking questions around responsible sourcing and corporate social responsibility (CSR) matters and that it can be a real competitive advantage to understand this and promote the work undertaken. This brings us neatly on to Fair Luxury, which in their own words is "an independent group of committed changemakers creating a platform to discuss and promote responsible sourcing in the jewellery industry." The group started in 2016 and for the first time were responsible for a series of talks and discussions at IJL which helped to promote this approach to the industry.

Shifting from the sourcing of material to manufacturing brings us to the two remaining factors. First looking at Skin Kind, this is an approach which M&S, the major UK retailer, has used on all its jewellery since May this year. This approach came in response to allergy concerns and was developed in conjunction with AnchorCert Group's testing laboratory in Birmingham, housed in the Birmingham Assay Office. The research uncovered 16 different metals most likely to cause a reaction including nickel. Legislation is already in place to protect customers, but both cobalt and chromium were also highlighted. M&S have consequently developed alternatives in their range and this approach has helped a significant upturn in sales from this retailer despite the shrinking UK market.

Finally we note the announcement that the National Association of Jewellers (NAJ) has formed a partnership with the Made in Britain brand. This will provide its members with the opportunity of a preferential rate in 2018. It is important to note that this is quite different from hallmarking, which remains obligatory for all items in the UK, even though the vast majority are imported (and sometimes hallmarked elsewhere too). Indeed, with the uncertainty around Brexit this could lead to the loss of the reciprocal arrangement that exists between assay offices in the region and hence force some importers to hallmark at one of the UK assay offices and exporters to shift some of their hallmarking overseas.

# THAILAND

- **Sellers re-emerge in Thailand as jewellery demand softens in the third quarter.**

Thai gold consumption in the third quarter was mixed, with an increase in investment demand partially offset by a stagnant jewellery sector. Following healthy investment demand in July sellers re-emerged in mid-September as prices in local terms traded at multi-month highs. Meanwhile, jewellery offtake was impacted by the rising price with a modest fall for the period.

Retail investment picked up strongly from the start of this quarter as domestic gold prices in early July bottomed at a seven month low of 20,116 baht per baht bar, encouraging aggressive restocking both from consumers and across the supply chain. This rise in activity was reflected in the surge in bullion imports in July, which at 37 tonnes was the highest of the year and was in fact the highest since November 2015. In 2016 bullion flows were dominated by exports as Thai investors took advantage of higher prices to liquidate gold holdings which pushed the market into surplus and as a result drove exports higher. Total imports last year stood at around 145 tonnes (a seven-year low) while exports surged to 176 tonnes, a level not seen since 2012.

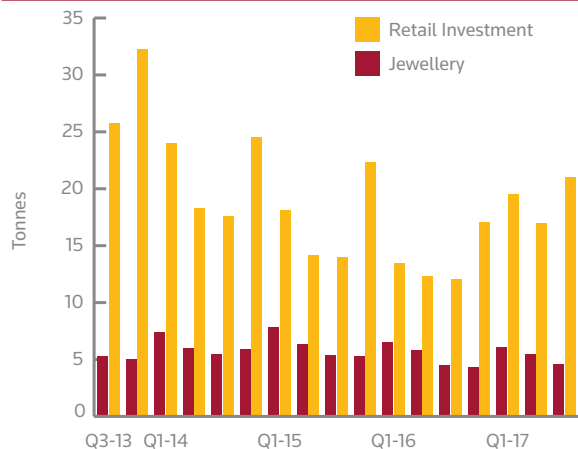
Turning to this year as a whole, investors have again had the upper hand for the most part with imports to end-July surpassing 145 tonnes, against 57 tonnes for the corresponding period last year. Switzerland has accounted for the majority of these flows at 57% of the total with Hong Kong, Singapore, and Australia sharing the bulk of the remainder. While there was this initial onslaught of demand in early July this soon dissipated as the baht gold price began to move higher, closing the month at over baht 20,500 per baht bar. Another brief correction in early August again provided another enticing entry point for investors but thereafter a rising price saw fresh demand ease as sellers again entered the market, providing for more or less a balanced market between the buy-side and sell-side traders.

The end of August and early September saw gold prices continue to track higher, influenced by the geo-political tensions on the Korean Peninsula, pushing gold in domestic terms above 21,700 per baht bar on 8th September, the highest level since November last year. Not surprisingly this generated a renewed wave of selling with Bangkok's Chinatown retail outlets flooded with customers wishing to sell back their earlier purchases, but with gold prices retreating from the highs so too did the rate of liquidations with many investors now waiting for the next rally for their opportunity. Nonetheless, the brief period of sell side activity was intense, limiting the overall growth in investment demand for the quarter as this selling pressure offset some of the earlier gains.

The jewellery sector also benefited from the lower price environment early in the quarter as restocking by retailers and a pick-up in export orders boosted fabrication volumes. Domestic consumption was also buoyant after declining by an estimated 7% in the first half of 2017, especially the higher purity (965) jewellery and ornament segment. However as with investment demand this too lost momentum as gold traded higher, softening considerably through August

and early September, dragging overall demand for the quarter into negative territory with a modest 3% decline forecast.

## THAILAND INVESTMENT AND JEWELLERY FABRICATION



Source: GFMS, Thomson Reuters

## THAILAND MARKET OUTLOOK

**Both jewellery and retail investment demand picked up again in late September and early October as gold traded below \$1,300 but offtake as been muted. A sizeable retracement in price would certainly encourage renewed retail activity as would a push above \$1,325 drive liquidation. The current trading band, however, is likely to stifle trade until a clearer signal is apparent with customers willing to wait for their opportunity to enter or exit the market.**



## JAPAN

- **Japanese investment demand influenced by Korean Peninsular tensions while jewellery consumption still lags.**

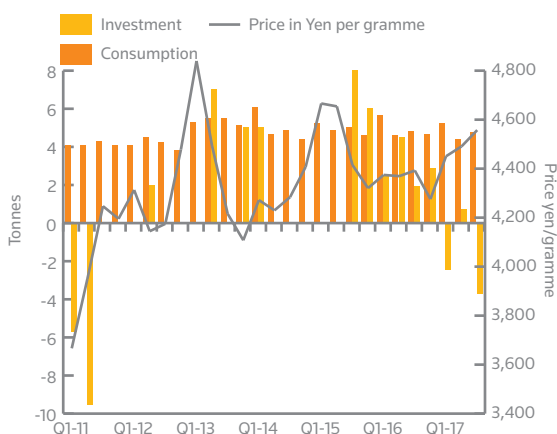
Japanese retail investment for gold suddenly roared back to life in September after eight months of inactivity. With gold in yen terms moving very little this year retail volumes have been underwhelming for the most part. However, this changed recently after the recent rise in tensions on the Korean Peninsula with safe haven purchases initially driving demand higher before an onslaught of sell-side activity. Meanwhile, jewellery consumption remains subdued and looks set for a decline this year unless demand rebounds in the final quarter of 2017, a scenario we think is unlikely given the current price level.

The recent tensions between North Korea and the West, and inflamed further by the launch of a ballistic missile that sailed over Northern Japan on the 28th August, pushed the gold price in yen terms on that day above 4,600 yen per gramme, a level not seen since March 2016. The sudden increase in price initially flushed out sellers who took advantage of the multi-month price peak to book profits. Interestingly, the momentum turned completely in subsequent days as gold continued to track higher due the increase in aggressive rhetoric from both sides which further inflamed the situation. The rise in tensions saw safe haven purchases emerge in Japan with demand for fresh metal surging briefly in early September, despite the yen price pushing through the 4,700 yen per gramme level before once again swinging back to disinvestment as the likelihood of military intervention dissipated. After a year of little activity in retail investment the market was suddenly buoyant again as consumers looked to lock in profits pushing demand for the quarter into net disinvestment of an estimated 3.7 tonnes.

Gold jewellery consumption in Japan this year has for the most part been flat to weaker with a modest decline expected for the full year after slipping 6% in the first six months. Demand in the third quarter was broadly stable before being influenced by the sudden rise in the yen gold price in September which curtailed retail sales for the full quarter dragging offtake for the period 1% below the corresponding period in 2016. The Japanese economy has been stronger this year and retail sales growth remains in a gradual recovery phase, but it has been difficult to maintain the high pace of growth seen earlier this year. Japan's retail sales growth slowed in July as shoppers spent less on clothes and cars and in August, which is typically the main holiday season, demand was impacted by unseasonably wet weather which is expected to weigh heavily on overall demand. Inbound tourism has continued to provide support to local retailers this year as the market continues to benefit from a weaker currency. According to the Japanese National Tourism Organisation (JNTO), the estimated number of international travellers to Japan in August reached 2.5 million, a year-on-year growth rate of 20.9%. The number of foreign visitors in the first eight months of 2017 climbed by 17.8% from the same period last year.

In terms of demand trends, gold continues to battle for market share with platinum with the latter continuing to trade at a discount to gold and widely regarded as the premium or more luxurious of the precious metals in Japan.

### JAPAN JEWELLERY AND INDUSTRIAL FABRICATION



Source: GFMS, Thomson Reuters

Even though platinum jewellery demand is also struggling to register growth in 2017 it is easily dominating overall offtake, especially so for wedding jewellery. The erosion in gold's market share has been most acute for white 18-carat gold although yellow gold has also been affected.

### JAPAN MARKET OUTLOOK

***Jewellery consumption is expected to benefit from the stronger domestic economy but higher prices will continue to be a significant drag. Meanwhile on the investment front, sellers still have the upper hand and we expect to see further months of net disinvestment towards year-end.***



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## UNITS USED

<b>troy ounce (oz) =</b>	31.1035 grammes
<b>tonne =</b>	1 metric tonne, 32,151 troy ounces
<b>carat =</b>	gold purity in parts per 24

- Unless otherwise stated, U.S. dollar prices and their equivalents are for the LBMA Gold Price PM.
- Unless otherwise stated, all statistics on gold supply and demand are expressed in terms of fine gold content.
- Throughout the tables, totals may not add due to independent rounding.

## ACKNOWLEDGEMENTS

The estimates shown in the *GFMS Gold Survey* and its quarterly updates for the main components of mine production, scrap, fabrication and investment demand are calculated on the basis of a detailed supply/demand analysis for each of the markets listed in the main tables. In the vast majority of cases, the information used in these analyses has been derived from visits to the countries concerned and discussions with local traders, producers, refiners, fabricators and central bankers. Although we also make use of public domain data where this is relevant, it is the information provided by our contacts which ultimately makes this *GFMS Gold Survey* unique. We are grateful to all of them.

