

DEVELOPMENT PERSPECTIVES OF THE GOLD MARKET AND THE TENDENCIES OF ITS CHANGES IN THE SITUATION OF WORLD FINANCIAL CRISIS

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Gold reserves are an important component of currency-financial segment of financial resources of the country. They are represented as high liquid assets that act as a guarantee of the discharge of foreign obligations by Russia. The bigger is the amount of gold and foreign currency reserves, the more reliable is the country for foreign investors and creditors. The authors of the article evaluate the Russian practice of making gold and foreign currency reserves and suggest the methods of its improvement.

In the strategic plan price and investment changes in gold market are various. World metallurgic complex though with a delay in comparison to other economic branches has to react on the facts of the influence of world crisis. Stock markets fluctuate about minimum indices; strong volatility of foreign exchange market remains, there is a high risk of a dramatic decrease of prices in the market of precious metals that are boosted by financial structures. That is why in such periods investors pay special attention to the safest instruments of keeping savings. Traditionally gold is among them, that is not only the "eternal" symbol of wealth, but also a really attractive asset.

In the situation of long-term development of world financial crisis it is possible to keep the increase of prices for precious metals till the year 2030.

Gold will always be an attractive instrument for investment. Statistics proves that in the period 2007-2009 there was a considerable change in the priorities of the use of yellow metal. The importance of gold used as an investment instrument has grown. In the last three years investment demand has grown from 16% to 34%, while the demand in industrial and jewelry production was gradually reducing from 14% to 9% and from 70% to 57% accordingly.

Gold miners of all countries continue to explore the reserves of gold mining. There are almost no rich gold fields in all countries, there are only the poor ones that are actively developed. All these factors cannot but influence the price of gold and the spheres of its use.

Depending on the level of prices the specialists determine the profitability of extraction. The price for selling gold became practically identical to the prime cost of gold extraction.

In the beginning of 2008 there was an impetuous growth of prices for gold. This was caused by the considerable decrease of American dollar in comparison to the main currencies because of the problems in American economy. Because of the big-scale crisis in world stock market many big players move their assets into commodity markets, and here gold market is a "safe cell".

In the end of 2008 dollar began to strengthen its position in relation to euro that is why the prices for gold were decreasing. Further on the dynamics of the cost of gold will directly depend on the microeconomic development of USA economy and consequently on the dynamics of dollar rate in relation to the main world currencies. The price of gold also depends on its volume and extraction as we see in the table (see table).

Global raw material metallurgic sector remains stable in the situation of crisis. This fact gives the opportunity for business to develop and plan for middle and long-term perspective.

The stability of branch development is mainly supported by saving the activity of metallurgy in Chinese Peoples Republic, South Korea, some countries of Asia and South America.

Russia occupies the third place; the Republic of South Africa and the USA are the leaders. It is necessary to point out that China is actively increasing its gold and foreign exchange reserves and according to its indices is coming

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Gold reserves for 01.01.2008 (t) and its average content in ledge (g/t) and placer (g/m³) ore

	Overall reserve	Share in the world, %	Confirmed reserves	Share in the world, %	Content in ledge ore	Content in placer
All over the world	111639	100	60409	100	-	-
Republic of South Africa	31000	27,8	16000	26,5	5,09	0,2
USA	10100	9	5600	9,3	1,7	0,25
Russia	8420	7,5	5700	9,4	3,73	0,8
China	5500	4,9	2600	4,3	2,8	0,17
Australia	5480	4,9	3330	5,5	2,1	0,3
Canada	4650	4,2	2500	4,1	2,7	0,55
Brazil	4110	3,7	520	0,9	3	1,1
Uzbekistan	3070	2,9	2070	3,4	2,3	0,3
Indonesia	3210	2,9	2870	4,8	3,5	0,2
Papua – New Guinea	3150	2,8	1920	3,2	2,7	0,5
Ghana	2870	2,6	1750	2,9	2,6	0,4
Chile	2580	2,3	1780	2,9	2,5	0,5
The Philippines	2220	2	1280	2,1	3,4	0,5
Peru	2070	1,9	1410	2,3	1,7	-

closer to Russia. Analyzing the table you can see that the difference of the reserves of the USA and Russia is 2000 t in favour of the first. Though Russia is the leader in mineral and raw material base, developed countries use their gold reserves more rationally. World financial crisis has decreased the volume of reserves in RF by more than one third from 563,6 billion dollars registered on 26.09.08 to 385,9 billion dollars - registered on 01.05.09.

According to the data of assay office the decrease of production in this industry in January 2009 was 38% in comparison with the same period last year. Present situation gives wonderful opportunity for jewelry branch to get rid of unfair companies. Then it will have an opportunity to become import replacing and export oriented. A certain range of problems should be solved for this. Firstly, it is high fiscal obligation. It does not give the opportunity to buy new equipment and precious stones in the necessary quantity. Nowadays Russia extracts 180 tons of gold per year and processes only 70 tons. To compare we can use India that processes 700 tons of gold a year, while it extracts only 3,5 tons. For the successive branch operation it is necessary to have such normative and legal base in our country that will correspond to similar bases existing in the countries-competitors.

Therefore the most probable development of gold market is the following: the slow-down of the US economy has already turned into recession that will last for about two or three

quarters. US economy will quickly come out of recession, but recovery will be longer - 2-3 years. In this case negative impact will remain longer, and dollar will be influenced by US statistics being close to the values of 1,5-1,6 dollar per euro. The price for gold will fluctuate in the limits of 1000-1100 dollars per troy ounce. Deteriorating macro economic US indices say in favour of this scenario. As it is difficult to evaluate the depth of possible recession objectively, this scenario can become the most real.

The lingering character of financial crisis will influence the distribution of the demand for gold. As a consequence of world cut of the companies of secondary sectors the tendency of cutting the demand in industrial production will remain. On the other hand, the desire to make yourself secure against global devaluation of assets will increase the percentage of investments in yellow metal.

There were two significant events in national gold mining branch in 2008. Firstly, a new big player appeared in Russian gold mining market «Polymetal» company. Earlier the company profile was silver production, however later together with the change of owners the company has changed its focus gold mining and production. By 20102011 «Polymetal» can become one of the biggest players in the branch.

Secondly, in 2007 2008 the processes of mergers and acquisitions strengthened. The brightest example is the acquisition of “Kazakhgold” by “Polyus Zoloto” JSC. This deal is very important for further strategic development

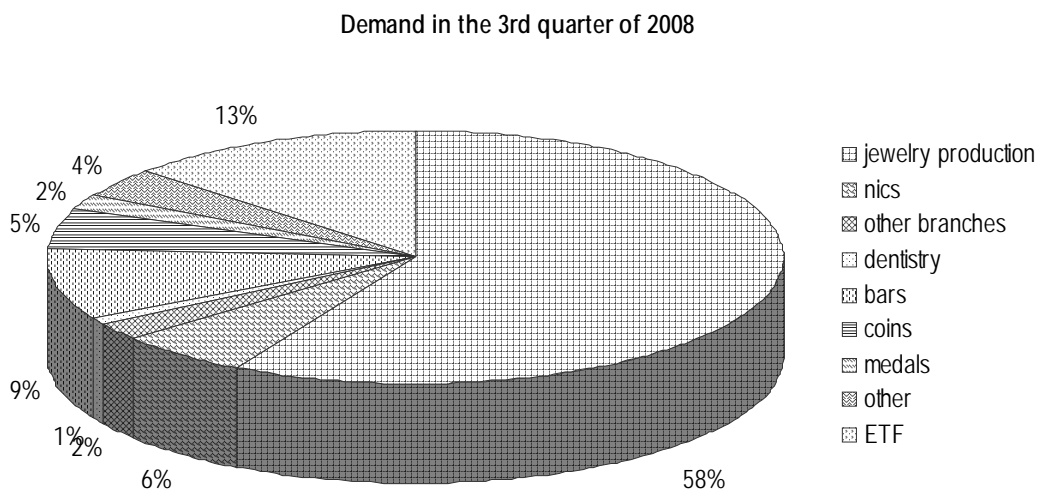
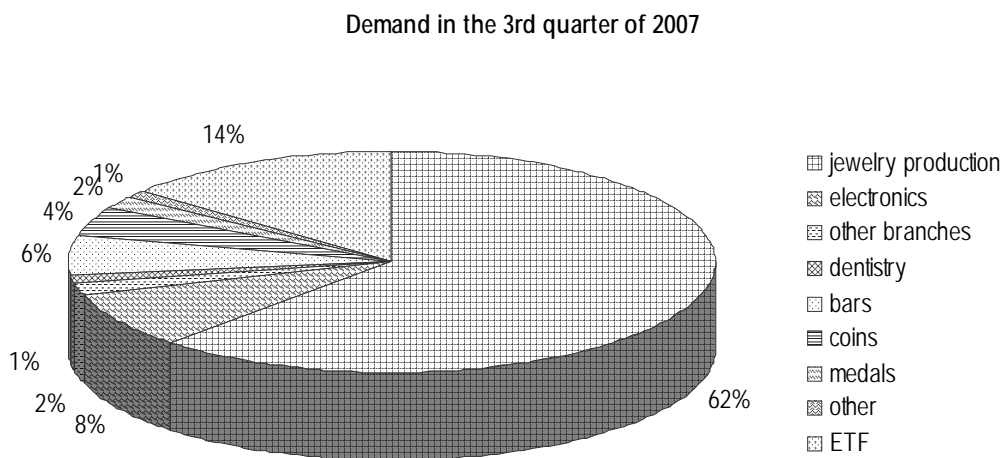
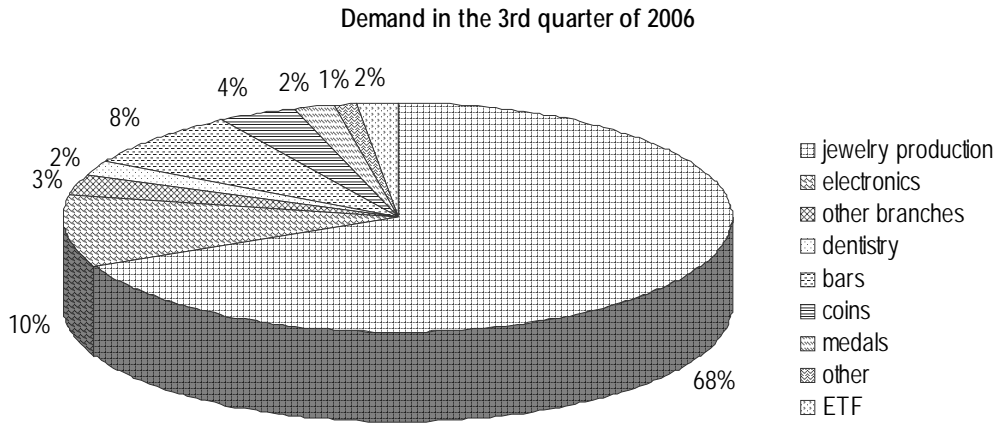


Fig. The dynamics of the demand for gold in the 3rd quarters of 2006-2008

of Russian gold mining. The only drawback is the high price of the deal. From the moment of making the deal concerning the acquiring of Kazakh company its market capitalization has decreased significantly. As a result "Polyus Zoloto" can pay the bonus of 500% to current

market price of "Kazakhgold", though initially the standard bonus of 4050% was suggested for control. For "Polyus Zoloto" the strategic importance of the deal is the following: Russian company has a very big resource base, however the level of mining is not high in comparison

to the overall resource base. The purchase of "Kazakhgold" will make it possible to increase the level of extraction by the year 2010 that will have a favorable influence on Russian gold mining business.

The crisis of financial liquidity influences the activity of Russian gold-mining companies as well as the activity of the whole real sector. The limitations on the access to credit resources made gold miners to impose the more detailed control over the costs and reconsider the investment program for 2009. In 2009 big gold-mining companies plan to continue the active policy of mergers and acquisitions and buy small companies of the sector. The authorities of "Polyus Zoloto" recently informed that the company is considering 22 assets as the possible aims for acquisition.

According to future forecast half of the income of RF budget will be still formed by the tax revenues of the companies operating in surface resource management, that is why the government will probably provide credits of Vnesheconombank to some metallurgy companies.

In short and middleterm perspective positive development of future producers are possible. "Polyus Zoloto" will increase the volume of production in the regions of its presence willing to be among the five world leaders of gold-mining. "Polymetal" JSC issued up to 280 thous. ounces of gold in 2008, and up to 300 thousand ounces in 2009 in the framework of partnership with Chinese Zijin Mining in Sverdlovsk region. According to the experts in the nearest three years the growth of gold mining in Krasnoyarsk region will be 42,1% - more than 45 tons of precious metal a year.

In December 2008 the auctions were held in Irkutsk region for choosing several participants of the subsurface in Bodaibinskiy region and lode gold in Jubilieinoe. The competition for gold minefield Sukhoi Log will take place in 2009.

"Ildikanzoloto" will start the construction of the second line of the factory in 2010 at Savkinskiy minefield in Zabaikalsk region that will increase gold production up to 2 tons a year.

"Polymetal" JSC will start the construction of floatation plant in Khabarovsk region in 2009 and ore mining and smelting complex in Amursk targeted at starting the launch of production till 2011.

"Artel stroiteley Amur" will start the development of gold ore deposit in Ayano-Mayskom region. The enterprises will be busy developing this deposit for about 10 years.

Therefore, the number of branches and segments of metallurgic business will suffer from negative factors. Some small and middle-scale companies can go bankrupt and therefore perspective players will amalgamate and this will help metallurgic sector to maintain attractiveness.

It will be possible to observe stable development in the sector of precious metals. Industrial indices will continue growing in China and Russia, against the depression of the players from the Republic of South Africa, Canada and Australia. Till the end of 2008 the prices for yellow metal will gradually increase, but in 2009 the growth of prices can stop and this will be followed by local correction of prices for precious metals.

In Russia the influence of the crisis will be softened by the presence of significant internal demand and own mineral and raw material base, as well as in the case of receiving timely, real, centralized and adequate government support. In the meanwhile it is suggested that company crediting will be accomplished optionally without taking into account the real state of affairs and development perspectives.

Revolutionary redistribution of internal market will take place that will draw off Russian players from the participation in foreign projects, especially in the regions with high potential of investment risks growth and tightening the competition.

Gold processing companies aspire to increase the volumes of extraction as the demand for production is growing and production costs are decreased in the situation of crisis. Therefore the struggle for the distribution of new perspective assets is expected.

It is forecasted that in Russia the stable growth of internal demands for metallurgy development will have a stable positive character. In the future there will be a practice of forming multiprofile alliances with foreign participation in order to have an excess to the biggest assets.

As for world gold-miners, financial crisis make them to reduce and even eliminate investment programs that in its turn will make it pos-

sible to make investments in developing and searching new deposits. Of course, this will be reflected in the decrease of the supply of metal to the market, such perspective is a long-term one. As for the middle-term perspective, there won't be any changes in supply. It would be possible partially to compensate the decrease by the secondary recycling of metal.

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