

The relevance of gold as a strategic asset

UK edition



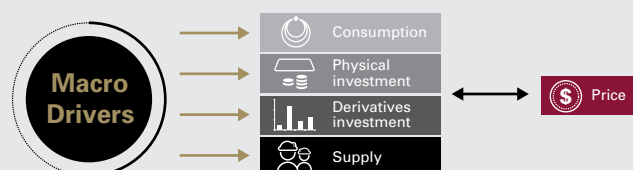
2021

How to value gold for maximum portfolio impact

Gold does not directly conform to the majority of the most common valuation methodologies used for equities or bonds. Without a coupon or dividend, typical models based on discounted cash flows, expected earnings, or book-to-value ratios, struggle to provide an appropriate assessment for gold's underlying value. This presented an opportunity for the World Gold Council to develop a framework to better understand gold valuation.

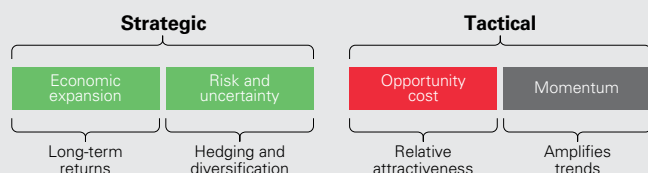
What is the Gold Valuation Framework (GVF)?

GVF is a methodology that allows investors to understand the drivers of gold demand and supply and, based on market equilibrium, estimate their impact on price performance. GVF powers our web-based tool, **Qaurum**SM, which allows users to assess the potential performance of gold under customisable hypothetical macroeconomic scenarios provided by Oxford Economics.¹



Our analysis shows that **the price performance of gold** can be explained by the interaction of four key drivers:

- **Economic expansion:** periods of growth are very supportive of jewellery, technology and long-term savings
- **Risk and uncertainty:** market downturns often boost investment demand for gold as a safe-haven
- **Opportunity cost:** the price of competing assets, especially bonds (through interest rates) and currencies, influences investor attitudes towards gold
- **Momentum:** capital flows, positioning and price trends can boost or dampen gold's performance.



For more information on **long-** and **short-term** drivers of gold, visit the **data** section on **Goldhub.com**

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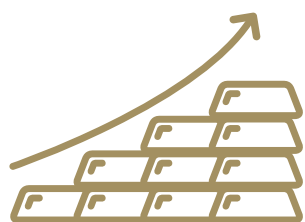
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¹ **Oxford Economics** is a leader in global forecasting and quantitative analysis and a specialist in modelling. Visit **Qaurum** for important disclosures about Oxford Economics' data, as well as a detailed description of the available scenarios; the assumptions underlying and data used for each scenario; and its respective hypothetical impact on gold demand, supply and performance

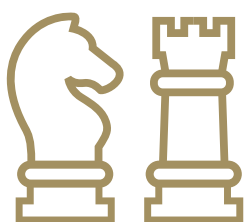
What makes gold a strategic asset?

Gold benefits from diverse sources of demand: as an investment, a reserve asset, jewellery, and a technology component. It is highly liquid, no one's liability, carries no credit risk, and is scarce, historically preserving its value over time.

Gold can enhance a portfolio in four key ways:



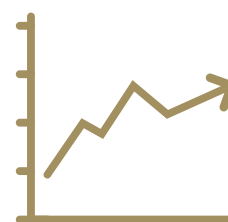
Returns



Diversification



Liquidity



**Portfolio
Performance**

Extraordinary times with extraordinary opportunities

2020 posed unprecedented challenges to investors as the first global pandemic in a century ravaged the world economically and socially.

COVID-19 significantly increased uncertainty by compounding existing risks and creating new ones. The rollout of new vaccines at the end of last year fuelled optimism that the worst was over. Yet the pandemic and the ensuing policy response from governments will likely have unintended consequences for, and create structural changes to, asset allocation strategies.

Global central banks have effectively taken interest rates to zero, driving nearly all sovereign debt to negative real yields. With less opportunity for yield across fixed income assets – especially those of shorter duration or higher quality – investors will likely continue to shift exposure to riskier assets. This has pushed many global stock markets to extreme levels on numerous valuation metrics and – importantly – has also served to increase the risk profile of most investment portfolios.

Additionally, many countries have made it clear they will continue to enact sizeable fiscal policy measures to tackle the economic impact of COVID-19, along with expanding budget deficits and balance sheets.

We believe these actions – in combination with the current environment have made gold increasingly relevant as a strategic asset. Not only could investors benefit from gold's role as a diversifier amid ballooning budget deficits, inflationary pressures, and potential market corrections from already high equity valuations, but they may also see additional support as gold consumption will likely benefit from the nascent economic recovery, especially in emerging markets (see *2021 Gold Outlook*).

ESG considerations

Over recent years, investors have increasingly looked to integrate environmental, social and governance (ESG) considerations as part of their investment process. For example, 89% of European investors now take ESG factors into account when they make investment decisions.² This increased emphasis on ESG reflects increasing pressure for businesses to actively manage ESG risks. It also emphasises that good ESG performance could lead to better long-term financial performance.³ This shift towards a greater integration has important implications for gold, which needs to demonstrate that it is produced and sourced responsibly, as well as the role that gold can play in supporting ESG objectives within a portfolio (**Focus 2: Gold as an ESG investment**).⁴

² Mercer, *European Asset Allocation Insights 2020*, August 2020.

³ Refinitiv, *How do ESG scores relate to financial returns*, August 2020.

⁴ *Gold and climate change: Current and future impacts*, October 2019.

Our analysis illustrates that adding between 5% and 13% in gold to a hypothetical UK pension fund average portfolio over the past decade would have resulted in higher risk-adjusted returns.⁸

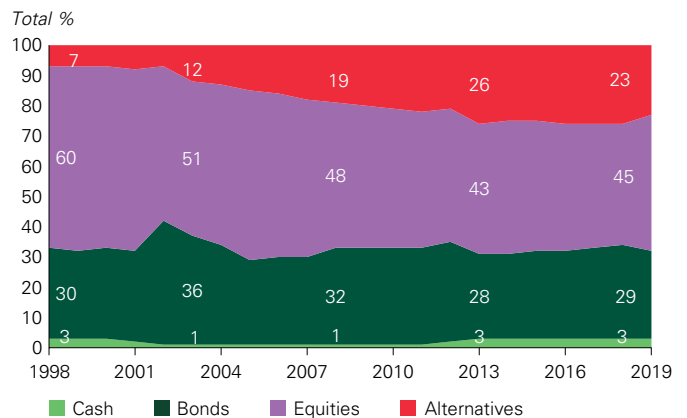
The increased relevance of gold

Institutional investors⁵ have embraced alternatives to traditional investments such as equities and bonds in pursuit of diversification and higher risk-adjusted returns. The share of non-traditional assets, such as hedge funds, private equity funds or commodities, among global pension funds increased from 7% in 1998 to 23% in 2019 – this figure is 30% in the US (**Chart 1**).⁶

Gold allocations have been recipients of this shift. Investors increasingly recognise gold as a mainstream investment; global investment demand has grown by an average of 15% per year since 2001 and the gold price has increased almost eight-fold over the same period.⁷

Chart 1: Alternative investments including gold have become a key portfolio strategy

Institutional investors continue to add alternative investments, including gold, to their portfolios*



*As of December 2019.

See **Willis Towers Watson, Global Pension Asset Study 2020**.

Source: Willis Towers Watson, World Gold Council

Gold performance has been strong in recent decades, supported by key structural changes

Monetary policy

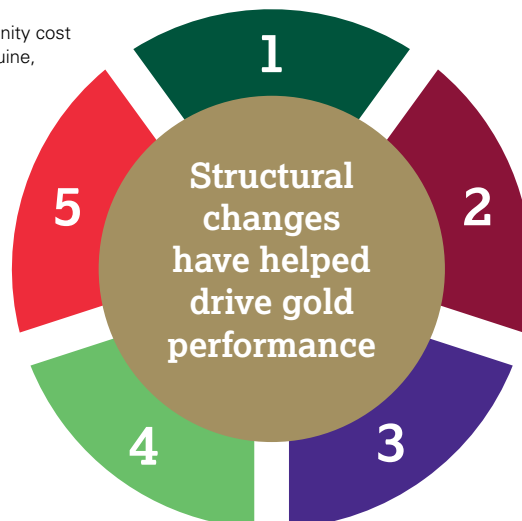
Persistently low interest rates reduce the opportunity cost of holding gold and highlight it as a source of genuine, long-term returns, particularly when compared to historically high levels of negative-yielding debt.

Emerging market growth

Economic expansion – particularly in China and India – increased and diversified gold's consumer and investor base.

Market access

Gold-backed ETFs have facilitated access to the gold market and materially bolstered interest in gold as a strategic investment, reduced total cost of ownership and increased efficiencies.



Central Bank Demand

A surge of interest in gold among central banks across the world, commonly used in foreign reserves for safety and diversification, has encouraged other investors to consider gold's positive investment attributes.

Market risk

The global financial crisis prompted a renewed focus on risk management and an appreciation of uncorrelated, highly liquid assets such as gold. Today, trade tensions and concerns about the economic and political outlook have encouraged investors to re-examine gold as a traditional hedge.

Source: World Gold Council

5 An institutional investor holds and/or manages assets for clients in larger, pooled portfolios often represented as mutual funds, banks, brokerages, hedge funds, etc.

6 Willis Towers Watson, *Global Pension Assets Study 2020*, February 2020 and *Global Alternatives Survey 2017*, July 2017.

7 Returns in pound sterling from 31 December 2000 to 31 December 2020.

8 See Chart 13 on p09 for more details behind the composition of the hypothetical UK pension fund average portfolio. Based on 2000 – 2020. In addition, refer to important disclaimers and disclosures at the end of this report.

Gold's strategic role

Our analysis shows gold is a clear complement to equities, bonds and broad-based portfolios. A store of wealth and a hedge against systemic risk, currency depreciation and inflation, gold has historically improved portfolios' risk-adjusted returns, delivered positive returns, and provided liquidity to meet liabilities in times of market stress.

A source of returns

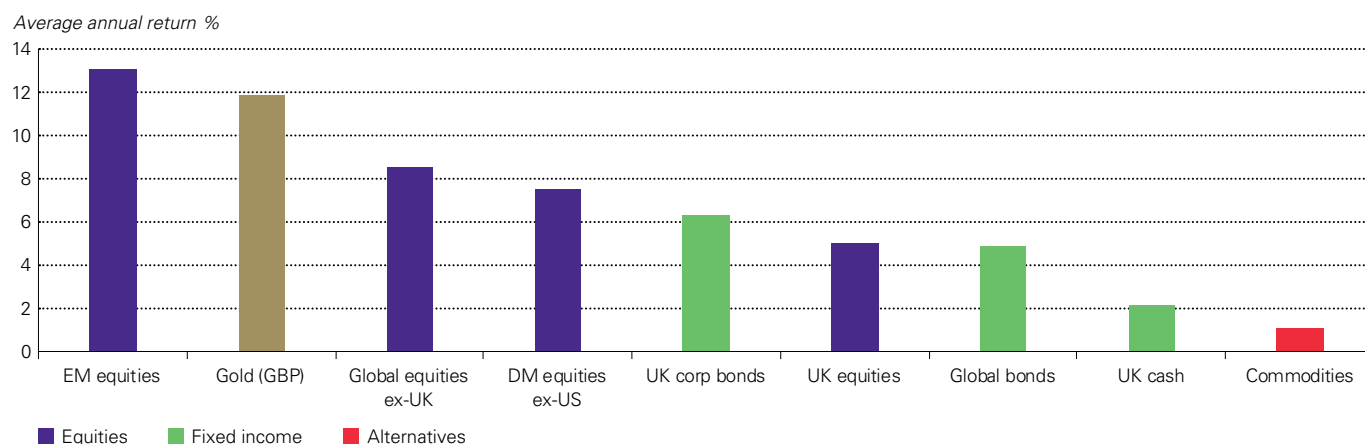
Investors have long considered gold a beneficial asset during periods of uncertainty. Historically, it has generated long-term positive returns in both good and bad economic times. Looking back almost half a century, the price of gold in US dollars has increased by an average of nearly 11% per year since 1971⁹ when the gold standard collapsed.¹⁰ Over this period, gold's long-term return is comparable to equities and higher than bonds.¹¹ Gold has also outperformed many other major asset classes over the past five, 10 and 20 years (**Chart 2**, **Chart 3**, p4).

This duality reflects the diverse sources of demand for gold and differentiates it from other investment assets. Gold is often used to protect and enhance wealth over the long term as it is no one's liability, and it operates as a means of exchange due to its global recognition.

Gold is also in demand via the jewellery market, valued by consumers across the world. And it is a key component in electronics.¹² These diverse sources of demand give gold a particular resilience: the potential to deliver solid returns in various market conditions (**Chart 7**, p6).

Chart 2: Gold has outperformed most broad-based portfolio components over the past two decades*

Average annual return of key global assets in pound sterling*



*Returns from 31 December 2001 to 31 December 2020.

Computations in British pound Spot of total return indices for LBMA Gold Price PM GBP, Barclays Benchmark Overnight GBP Cash Index, S&P U.K. Investment Grade Corporate Bond Index Total Return, Bloomberg Barclays Global-Aggregate Total Return Index Value Unhedged USD, FTSE All-World ex UK Total Return Index GBP, MSCI Daily TR Gross EM USD, MSCI ACWI ex USA Gross Total Return USD Index, FTSE 100 Total Return Index GBP, Bloomberg Commodity Index Total Return.

On Goldhub.com see: [Gold returns](#).

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

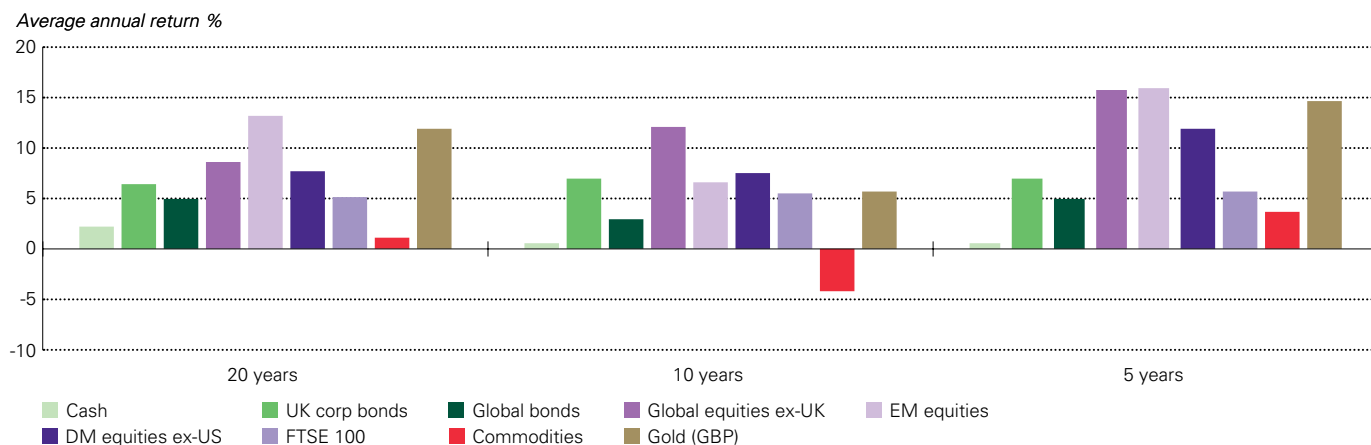
⁹ January 1971 – December 2020.

¹⁰ During the gold standard, the US dollar was backed by gold, and the foreign currency exchange rates were dictated by the Bretton Woods System. In August 1971, the Nixon Administration announced the halt of the free conversion between the US dollar and gold catalysing the collapse of the gold standard and, subsequently, the Bretton Woods system.

¹¹ For other return metrics and performance see Appendix II on p19.

¹² See Chart 20a, on p17.

Chart 3: Gold has performed well over the past decade, despite the strong performance of risk assets
Average annual return over the past five and 10 years*



*Returns in pound sterling from 31 December 2010 to 31 December 2020.
See **Chart 2** for respective indices.

On Goldhub.com see: **Gold returns**.

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

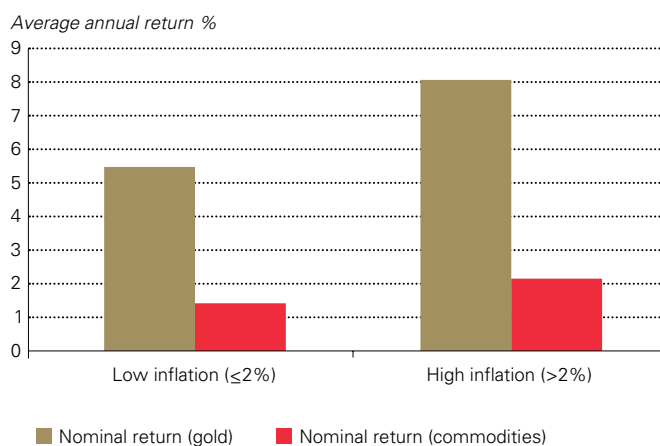
Beating inflation, combating deflation

Gold has long been considered a hedge against inflation and the data confirms this. The average annual return of 11% in US dollars over the past 50 years, has outpaced the UK and world consumer price indices (CPI).¹³

Gold also protects investors against high and extreme inflation. In years when inflation was higher than 2%, gold's price increased 8% per year on average (**Chart 4**). Over the long term, therefore, gold has not just preserved capital but helped it grow.

Research also shows that gold should do well in periods of deflation.¹⁴ Such periods are characterised by low interest rates, reduced consumption and investment, and financial stress, all of which tend to foster gold demand.

Chart 4: Gold historically rallies in periods of high inflation, outperforming broad-based commodities
Gold and commodity returns in pound sterling as a function of annual inflation*



*Based on y-o-y changes for the LBMA Gold Price PM, Bloomberg Commodity Index and UK CPI between December 1988 and 31 December 2020 in pound sterling, based on available data.

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

¹³ Based on average annual CPI changes for the US (3.9%) and world (9.3%) as measured by the IMF from December 1971 – December 2020.

¹⁴ Oxford Economics, *The impact of inflation and deflation on the case for gold*, July 2011.

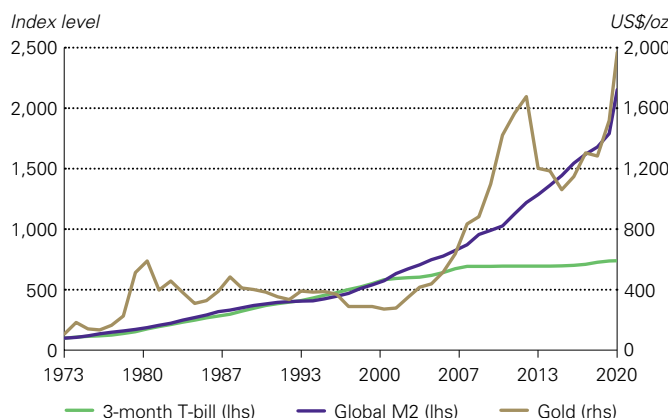
Outperforming fiat currencies

Investor demand has been boosted by persistently low interest rates and concerns about the outlook for the dollar, which affect the perceived opportunity cost of holding gold.

Historically, major currencies were pegged to gold. That changed with the unravelling of the US gold standard in 1971 and the eventual collapse of the Bretton Woods system.¹⁵ Since then, with few exceptions, gold has significantly outperformed all major currencies and commodities as a means of exchange (**Chart 5**). This outperformance was particularly marked immediately after the end of the gold standard. A key factor behind this robust performance is that the supply growth of gold has changed little over time – increasing by approximately 1.4% per year over the past 20 years.¹⁶

By contrast, fiat money can be printed in unlimited quantities to support monetary policy, as exemplified by the quantitative easing measures in the aftermath of the Global Financial Crisis (GFC).¹⁷ In recent years, the rapidly increasing global money supply and a low to negative rate environment have fostered an optimal environment for gold to outperform global sovereign debt, such as US treasuries and to track the global money supply (**Chart 6**).

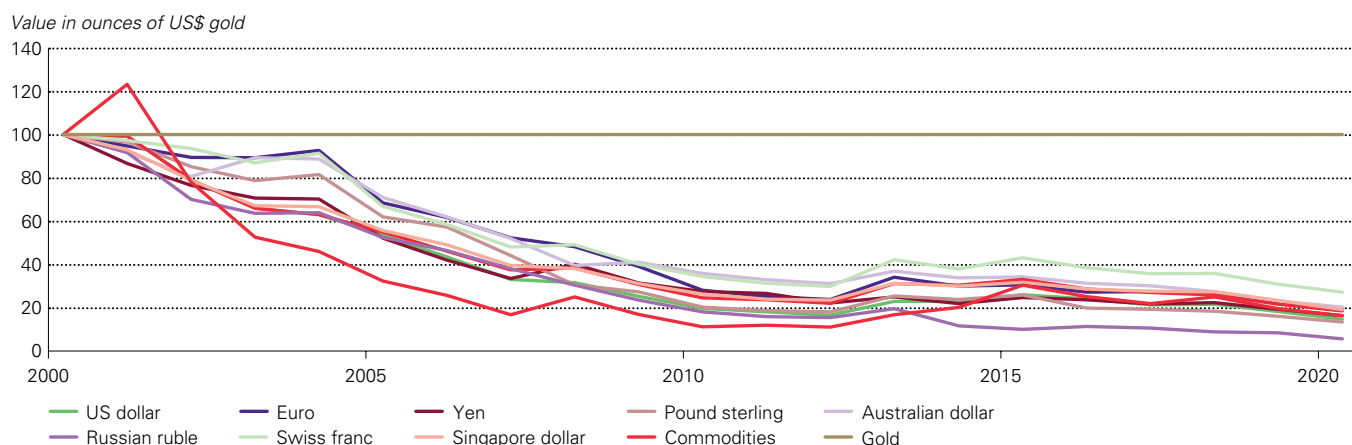
Chart 6: Gold prices have tracked the expansion of global money supply and outpaced T-bills over time
Global M2 growth, US 3m T-bill total return, gold price*



*As of 31 December 2020. Data starts in 1973 due to data availability. Global M2 is first calculated by aggregating the available universe of individual country M2 in US dollars (excluding Venezuela due to data quality) as provided by Oxford Economics. The resulting aggregate is then re-based to 100 on January 1973. US 3m T-bill total returns constructed using cumulative returns based on 3-month US T-bill yields and also rebased to 100 on January 1973. Gold based on the LBMA Gold Price PM USD.

Source: Bloomberg, ICE Benchmark Administration, Oxford Economics, World Gold Council

Chart 5: The purchasing power of major currencies and commodities has significantly eroded relative to gold
Value of currencies and broad commodities relative to gold (January 2000 = 100)*



*As of 31 December 2020. Relative value between the LBMA Gold Price PM, Bloomberg Commodity Index and major currencies since 2000. Value of currencies measured in ounces of gold and indexed to 100 in January 2000.

On Goldhub.com see: **Gold prices**.

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

¹⁵ Ibid footnote 10.

¹⁶ From 31 December 2000 – 31 December 2020. See the *Demand and Supply* section at Goldhub.com.

¹⁷ For more information please see *The impact of monetary policy on gold* and *It may be time to replace bonds with gold*.

Diversification that works

The benefits of diversification are widely acknowledged – but it is hard to find effective diversifiers. Many assets become increasingly correlated as market uncertainty rises and volatility is more pronounced, driven in part by risk-on/risk-off investment decisions. As a result, many so-called diversifiers fail to protect portfolios when investors need them most.

Gold is different in that its negative correlation to equities and other risk assets generally increases as these assets sell off (**Chart 7**). The GFC is a case in point. Equities and other risk assets tumbled in value, as did hedge funds, real estate and most commodities, which were long deemed portfolio diversifiers. Gold, by contrast, held its own and increased in price, rising 74% in pound sterling from December 2007 to February 2009.¹⁸ And in the most recent sharp equity market pullbacks of 2018 and 2020, gold performance remained positive.¹⁹

This robust performance is perhaps not surprising. With few exceptions, gold has been particularly effective during times of systemic risk, delivering positive returns and reducing overall portfolio losses (**Chart 8**, p7). Importantly too, gold allows investors to meet liabilities when less liquid assets in their portfolio are difficult to sell, or possibly mispriced.

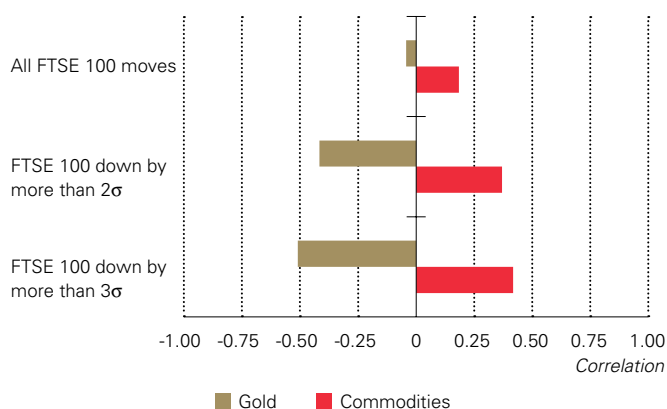
But gold's correlation does not just work for investors during periods of turmoil. It can also deliver positive correlation with equities and other risk assets in positive markets, making gold a well-rounded efficient hedge (**Chart 9**, p7), (see [Gold: an efficient hedge](#)).

This dual benefit arises from gold's dual nature: as both an investment and a consumer good (**Chart 20**, p17). As such, the long-term performance of gold is supported by income growth. Our analysis bears this out, showing that when equities rally strongly, their correlation to gold can increase. This is most likely driven by a wealth-effect supporting gold consumer demand, as well as demand from investors seeking protection against higher inflation expectations.

Gold has consistently benefited from 'flight-to-quality' inflows during periods of heightened risk.

Chart 7: Gold has been more negatively correlated with equities in extreme market selloffs than commodities

Correlation between gold, commodities, and UK equity returns in various environments of equity market performance since 1971*



*As of 31 December 2020. Correlations computed using weekly returns in pound sterling based on the Bloomberg Commodity Index and the LBMA Gold Price PM since January 1971 due to availability of data. The top bar corresponds to the unconditional correlation over the full period. The middle bar corresponds to the correlation conditional on FTSE 100 weekly return falling by more than two standard deviations (or 'σ') respectively, while the bottom bar corresponds to the FTSE 100 weekly return decreasing by more than three standard deviations. The standard deviation is based on the same weekly returns over the full period.

On Goldhub.com see: [Gold correlation](#).

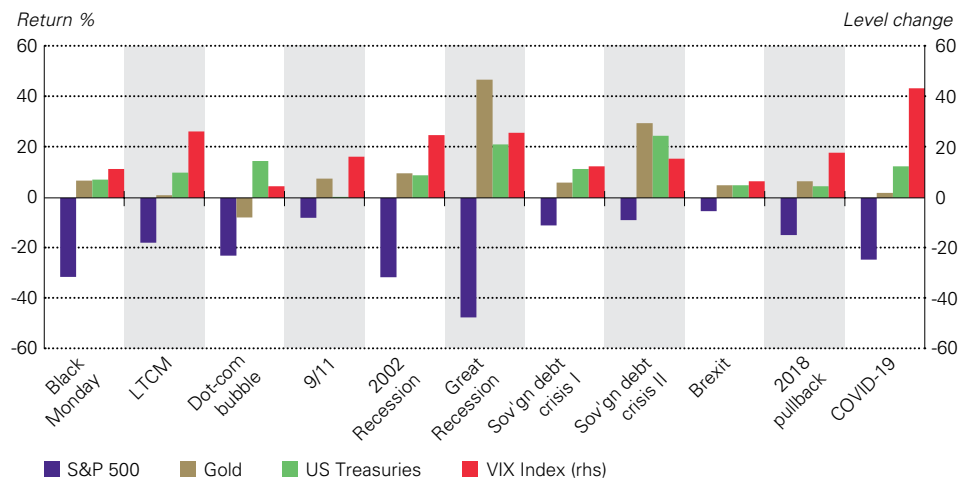
Source: Bloomberg, ICE Benchmark Administration, World Gold Council

18 Based on the LBMA Gold Price PM from 1 December 2007 to 27 February 2009.

19 Based on the LBMA Gold Price PM from 1 October 2018 to 27 December 2018 and from 31 January 2020 to 31 March 2020.

Gold behaves –
and is used – as
a safe-haven
in periods of
systemic risk...

Chart 8: The gold price tends to increase in periods of systemic risk
US equities, treasuries and gold versus the VIX index*



*The VIX is available only after January 1990. Returns in US dollars. For events occurring prior to that date annualised 30-day S&P 500 volatility is used as a proxy. Dates used: Black Monday: 9/1987 - 11/1987; LTCM: 8/1998; Dot-com: 3/2000 - 3/2001; September 11: 9/2001; 2002 recession: 3/2002 - 7/2002; Great Recession: 10/2007 - 2/2009; Sovereign debt crisis I: 1/2010 - 6/2010; Sovereign debt crisis II: 2/2011 - 10/2011; Brexit: 23/6/2016 - 27/6/2016; 2018 pullback: 10/2018 - 12/2018; COVID-19: 31/1/2020 - 31/3/2020.

Source: Bloomberg, World Gold Council

Asset	Performance during market sell-off*		Performance during market recovery*	
	Average	Median	Average	Median
Gold	10%	7%	25%	6%
US treasuries	11%	10%	13%	5%

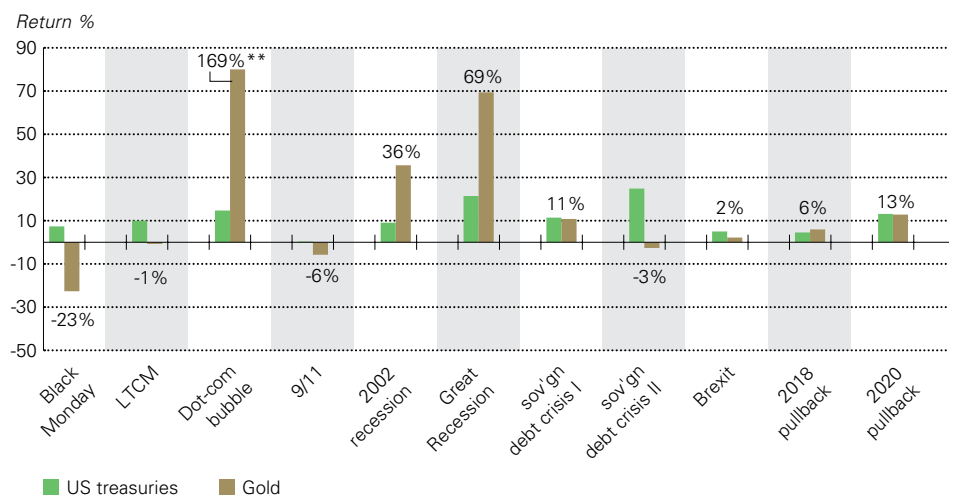
*Average and median returns based on time horizons in **Chart 8** and **Chart 9**.

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

...but also
performs well
in market
recoveries.

Chart 9: Gold prices perform well following the period after a systemic selloff and its subsequent recovery

Performance of gold and treasuries from the market trough (bottom) to the market recovery point (equity market levels before the systemic selloff)



* Returns in US dollars. Dates used are based off the end dates of **Chart 8**. Black Monday: 11/1987 - 6/1989; LTCM: 8/1998 - 11/1998; Dot-com: 3/2001 - 5/2007; September 11: 9/2001 - 11/2001; 2002 recession: 7/2002 - 11/2004; Great Recession: 2/2009 - 1/2013; Sovereign debt crisis I: 6/2010 - 10/2010; Sovereign debt crisis II: 10/2011 - 2/2012; Brexit: 6/2016 - 7/2016; 2018 pullback: 12/2018 - 6/2019; 2020 pullback: 3/2020 - 7/2020.

** The bar is truncated for the Dot-com bubble recovery due to its extreme differential between others and visibility.

Source: Bloomberg, World Gold Council

A deep and liquid market

The gold market is large, global and highly liquid.

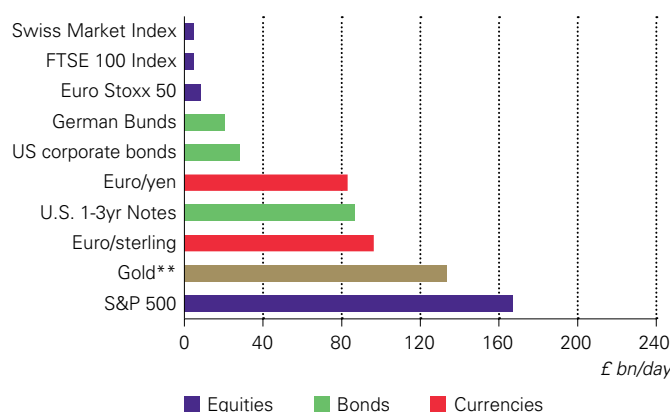
We estimate that physical gold holdings by investors and central banks are worth approximately £3.5 trillion (trn), with an additional £846 billion (bn) in open interest through derivatives traded on exchanges or the over-the-counter (OTC) market (**Chart 18a**, p16).

The gold market is also more liquid than several major financial markets, including US T-bills, euro/yen and UK Gilts, while trading volumes are similar to those of the S&P 500 (**Chart 10**). Gold's trading volumes averaged approximately £131bn per day in 2020. During that period, OTC spot and derivatives contracts accounted for £81bn and gold futures traded £51bn per day across various global exchanges. Gold-backed ETFs (gold ETFs) offer an additional source of liquidity, with the largest US-listed funds trading an average of £2.4bn per day (**Chart 11**).

The scale and depth of the market mean that it can comfortably accommodate large, buy-and-hold institutional investors. In stark contrast to many financial markets, gold's liquidity does not dry up, even at times of financial stress, making it a much less volatile asset (**Chart 12**).

Chart 10: Gold trades more than many other major financial assets

One-year average trading volumes of various major assets in pound sterling *



* Average daily volumes from 31 December 2010 to 31 December 2020, except for currencies that correspond to March 2019 volumes due to data availability.

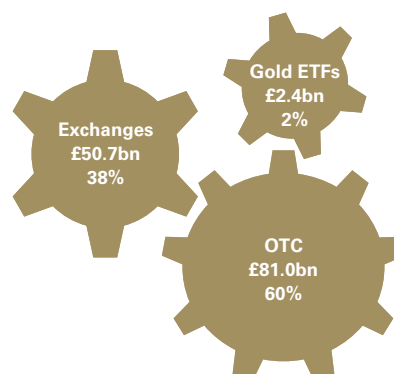
** Gold liquidity includes estimates of OTC transactions and published statistics on futures exchanges, and gold-backed exchange-traded products.

On Goldhub.com see: [Gold trading volumes](#).

Source: Bloomberg, Bank for International Settlements, UK Debt Management Office (DMO), Germany Finance Agency, Japan Securities Dealers Association, Nasdaq, World Gold Council

Chart 11: Gold is liquid across key investment platforms

Average daily trading volume by point of access in 2020*

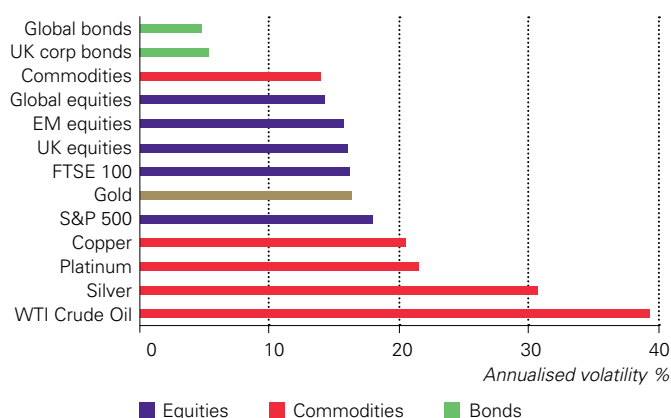


*Average daily trading volume from 1 January 2020 to 31 December 2020. Gold liquidity includes estimates of over-the-counter (OTC) transactions and published statistics on futures exchanges, and gold-backed exchange-traded products. For more information, see [Gold trading volumes](#) on [Goldhub.com](#).

Source: Bloomberg, Nasdaq, World Gold Council

Chart 12: Gold has been less volatile than many equity indices, alternatives and commodities because of its scale, liquidity and diverse sources of demand

Average daily volatility of several major assets since 2000*



*Annualised volatility is computed based on daily returns in pound sterling between 31 December 2000 and 31 December 2020. Computations of total return indices for S&P 500 Index, MSCI Daily Gross EM, MSCI Daily Gross EAFE, LBMA Gold Price PM, Bloomberg Commodity Index, LBMA Silver Price, Bloomberg WTI Crude Oil, Bloomberg Barclays Global-Aggregate Index, S&P GSCI Copper Official Close Index, S&P GSCI Platinum Index, Bloomberg Barclays Global-Aggregate Total Return Index Value Unhedged, MSCI UK Gross Total Return Local Index, S&P U.K. Investment Grade Corporate Bond Index Total Return.

On Goldhub.com see: [Gold volatility](#).

Source: Bloomberg, CBOE, COMEX, World Gold Council

Enhanced portfolio performance

Long-term returns, liquidity and effective diversification all benefit overall portfolio performance. In combination, they suggest that the addition of gold can materially enhance a portfolio's risk-adjusted returns.

Our analysis of investment performance over the past five, 10 and 20 years underlines gold's positive impact on an institutional portfolio. It shows that the UK pension fund average portfolio would have achieved higher risk-adjusted returns and lower drawdowns if 5%, 7.5% or 12.5% were allocated to gold (**Chart 13** and **Table 1**). This positive impact has been particularly marked since the GFC.

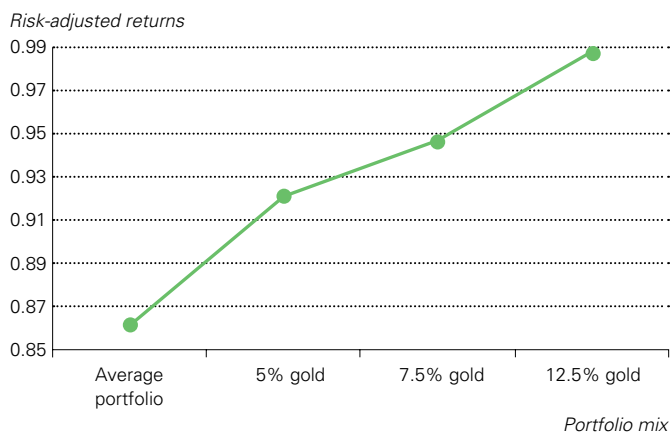
In addition to traditional back-testing, a more robust optimisation analysis based on 're-sampled efficiency'²⁰ suggests that an allocation to gold may result in a material enhancement to portfolio performance. For example, gold allocations between 5% and 12.5% across well-diversified pound sterling-based portfolios with varying levels of risk could result in higher risk-adjusted returns (**Chart 14**, p10).

The 'optimal' amount of gold varies according to individual asset allocation decisions. Broadly speaking, the analysis suggests that the higher the risk in the portfolio – whether in terms of volatility, illiquidity or concentration of assets – the larger the required allocation to gold, within the range in consideration, to offset that risk (**Chart 14**, p10).

Our analysis also indicates that gold's optimal weight in these hypothetical portfolios can be statistically significant even if investors assume an annual return for gold of between 2% and 4% – well below long-term historical performance. This works equally for investors who already hold other inflation-hedging assets, such as inflation-linked bonds,²¹ and for investors who hold alternative assets, such as real estate, private equity and hedge funds.²²

Chart 13: Adding gold over the past twenty years would have increased risk-adjusted returns of a hypothetical UK pension fund portfolio

Performance of a hypothetical UK pension fund (PF) average portfolio with and without gold*



*Based on monthly total returns from December 2000 to December 2020. The hypothetical average UK pension fund portfolio is based on Willis Tower Watson Global Pension Assets Study 2019 and Global Alternatives Survey 2017. Each hypothetical portfolio composition is roughly equivalent to the portfolio in Chart 14 and reflects a percentage in stock (Eqty), alternative assets (Alts), cash and bonds (FI). For example: the average pension allocation includes quarterly-rebalanced total returns of a 30% allocation to stocks (8% FTSE 100 Index, 22% FTSE All-World ex UK), 49% allocation to fixed income (13% Barclays UK Govt Inflation-Linked All Maturities Index, 11% Barclays Sterling Gilts Index, 10% S&P UK Investment Grade Corporates Index, 10% Barclays Global Aggregate Corporate Bonds, 3% Barclays EM Bond Index, 2% Barclays Overnight GBP Index), and 21% alternative assets (8% HFRI Hedge Fund Index, 7% FTSE EPRA Nareit Developed Europe Index, 6% LPX Europe Listed Private Equity Index). The allocation to gold comes from proportionally reducing all assets. The optimal gold allocation is added to the 'Alts' bucket. Risk-adjusted returns are calculated as the annualised return/annualised volatility. Analysis based on New Frontier Advisors Resampled Efficiency. For more information see Efficient Asset Management: A Practical Guide to Stock Portfolio Optimization and Asset Allocation, Oxford University Press, January 2008. Risk-adjusted returns are calculated as the annualised return/annualised volatility. See important disclaimers and disclosures at the end of this report.

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

Table 1: Gold has increased risk-adjusted returns while reducing portfolio volatility and maximum drawdowns

Comparison of an hypothetical average European investment portfolio and an equivalent portfolio with 10% gold over the past one, five, 10 and 20 years based on euros returns*

	20-year		10-year		5-year		1-year	
	No gold	5% gold	No gold	5% gold	No gold	5% gold	No gold	5% gold
Annualised return	6.6%	6.9%	7.6%	7.5%	8.8%	9.2%	10.7%	11.1%
Annualised volatility	7.7%	7.5%	6.7%	6.6%	7.5%	7.3%	9.4%	8.9%
Risk-adjusted returns	.861	.921	1.12	1.13	1.18	1.25	1.14	1.25
Maximum drawdown	-19.2%	-16.2%	-10.0%	-9.1%	-10.0%	-9.1%	-10.0%	-9.1%

*As of 31 December 2020. The hypothetical PF average portfolio and weights are based on Willis Towers Watson Global Pension Assets Study 2019 and Global Alternatives Survey 2017 and as described in **Chart 13**. Risk-adjusted returns are calculated as the annualised return/annualised volatility. Maximum drawdown is calculated as the largest fall in a portfolio before the total value reaches a previous peak.

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

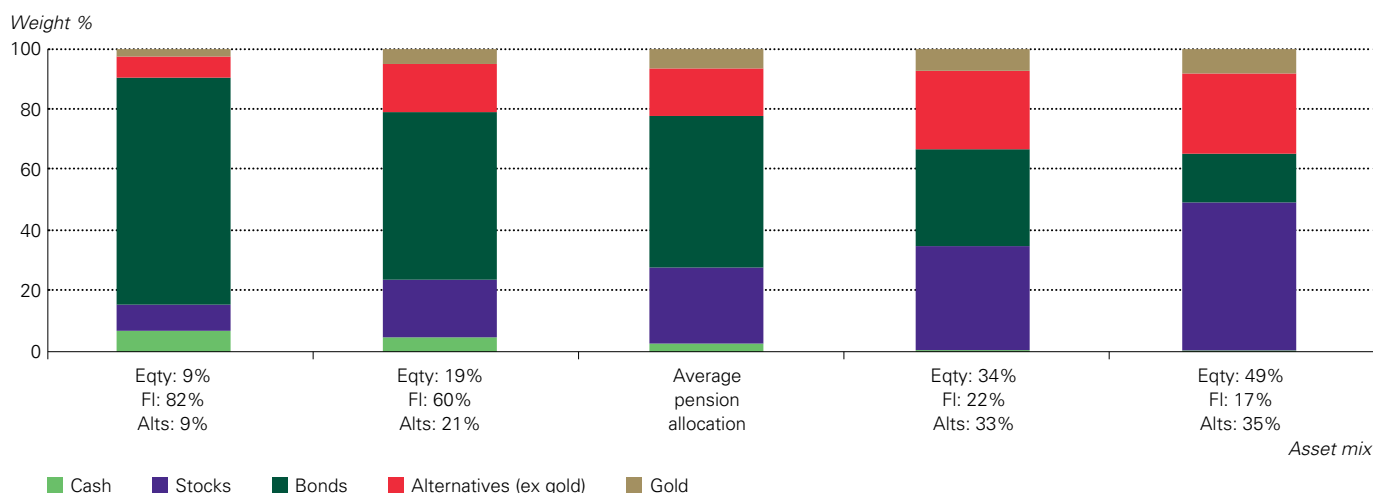
20 Re-sampled efficiency is a methodology developed by Richard and Robert Michaud and praised as a robust alternative to traditional mean-variance optimisation. See *Efficient Asset Management: A Practical Guide to Stock Portfolio Optimization and Asset Allocation*, Oxford University Press, January 2008.

21 *Gold as a tactical inflation hedge and long-term strategic asset*, July 2009.

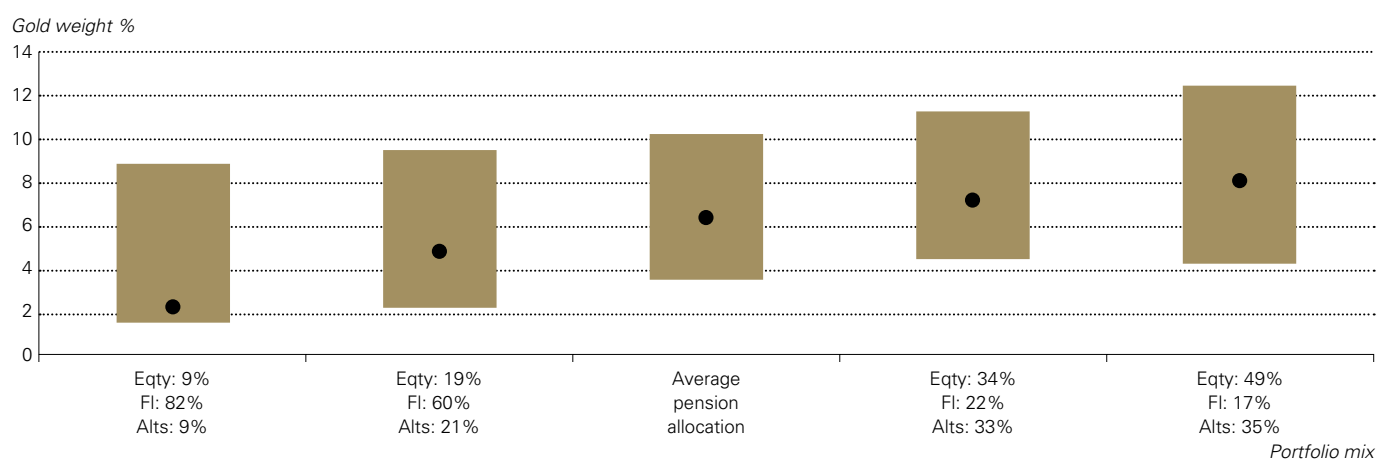
22 *Enhancing the performance of alternatives with gold*, February 2018.

Chart 14: Gold could significantly improve risk-adjusted portfolio returns across various levels of risk

(a) Long-run optimal allocations based on asset mix*



(b) Range of gold allocations and the allocation that could deliver the maximum risk-adjusted return for each hypothetical portfolio mix*



* Based on monthly total returns from December 1999 to December 2019. The hypothetical average UK pension fund portfolio is based on Willis Tower Watson Global Pension Assets Study 2019 and Global Alternatives Survey 2017. Each hypothetical portfolio composition is roughly equivalent to the portfolio in **Chart 14** and reflects a percentage in stock (Eqty), alternative assets (Alts), cash and bonds (FI). For example: the average pension allocation includes quarterly-rebalanced total returns of a 30% allocation to stocks (8% FTSE 100 Index, 22% FTSE All-World ex UK), 49% allocation to fixed income (13% Barclays UK Govt Inflation-Linked All Maturities Index, 11% Barclays Sterling Gilts Index, 10% S&P UK Investment Grade Corporates Index, 10% Barclays Global Aggregate Corporate Bonds, 3% Barclays EM Bond Index, 2% Barclays Overnight GBP Index), and 21% alternative assets (8% HFRI Hedge Fund Index, 7% FTSE EPRA Nareit Developed Europe Index, 6% LPX Europe Listed Private Equity Index). The allocation to gold comes from proportionally reducing all assets. The optimal gold allocation is added to the 'Alts' bucket. Risk-adjusted returns are calculated as the annualised return/annualised volatility. Analysis based on New Frontier Advisors Resampled Efficiency. For more information see *Efficient Asset Management: A Practical Guide to Stock Portfolio Optimization and Asset Allocation*, Oxford University Press, January 2008.

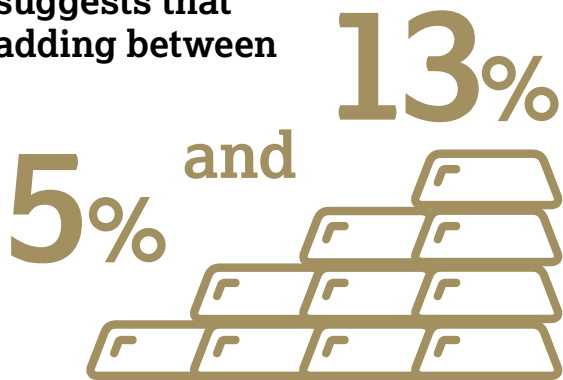
Source: World Gold Council

Conclusion

Perceptions of gold have changed substantially over the past two decades, reflecting increased wealth in the East and a growing worldwide appreciation of gold's role within an institutional investment portfolio.

Gold's unique attributes as a scarce, highly liquid, and uncorrelated asset demonstrate that it can act as a diversifier over the long term. Gold's position as an investment and a luxury good has allowed it to deliver average returns of nearly 11% over the past 50 years, comparable to equities and more than bonds and commodities.^{23,24}

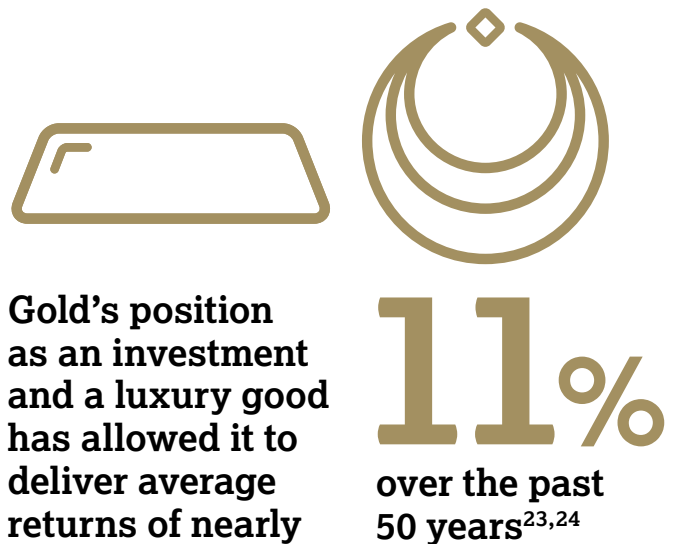
Extensive analysis suggests that adding between



of gold to a UK-based portfolio can make a tangible improvement to performance and boost risk-adjusted returns on a sustainable, long-term basis.²⁵

Gold's traditional role as a safe-haven asset means it comes into its own during times of high risk. But gold's dual appeal as an investment and a consumer good means it can generate positive returns in good times too. This dynamic is likely to continue, reflecting ongoing political and economic uncertainty, persistently low interest rates and economic concerns surrounding equity and bond markets.

Overall, extensive analysis suggests that adding between 5% and 13% of gold to a UK-based portfolio can make a tangible improvement to performance and boost risk-adjusted returns on a sustainable, long-term basis.²⁵



Gold's position as an investment and a luxury good has allowed it to deliver average returns of nearly

11% over the past 50 years^{23,24}

²³ Average annualised returns in US dollars from January 1971 to December 2020.

²⁴ See Chart 24, p19.

²⁵ See Chart 13, p9.

Focus 1: Gold – Not your average commodity

Gold is often part of the broad commodity complex: as a component of a commodity index, a holding in an ETF, or a future trading on a commodity exchange. While gold shares some similarities with commodities, there are several important differences:

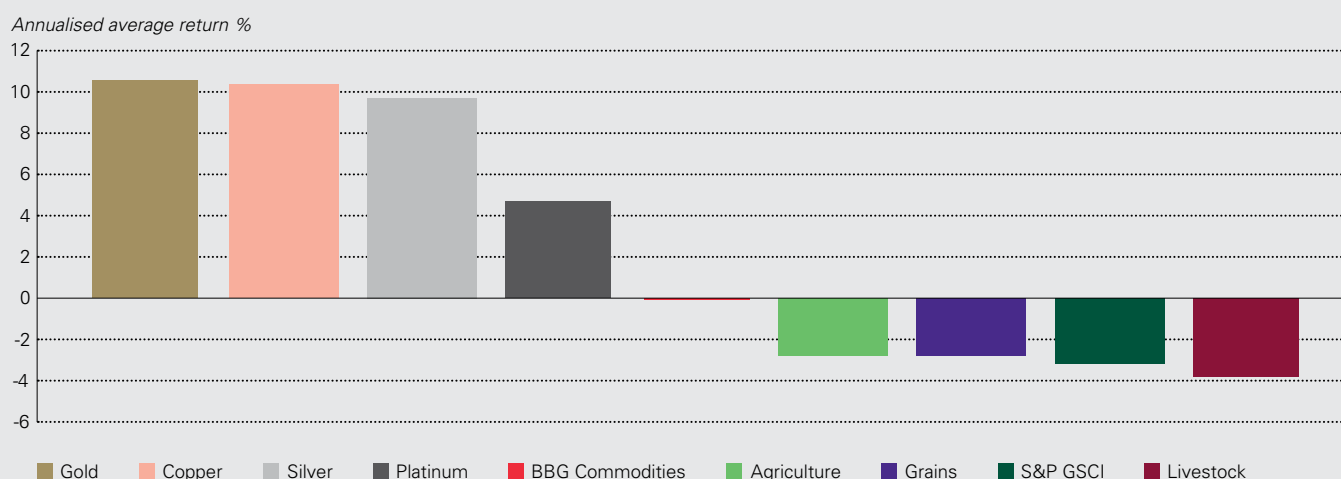
- gold is traditionally seen as a safe-haven asset
- gold is both an investment and a consumer good
- the supply of gold is balanced, deep and broad
- gold does not degrade over time, unlike most traditional commodities.

These attributes set gold apart from the commodity complex. And our research suggests that a distinct allocation to gold could enhance the performance of portfolios with passive commodity exposures.²⁶

Recently, developments in the performance and liquidity of gold have led two major commodity indices (S&P GSCI and Bloomberg Commodity Indices) to increase their weighting of gold for a second year in a row.²⁷ In 2020, gold had the largest individual commodity weight increase in the S&P GSCI Index and will have its highest weight ever in the Bloomberg Commodity Index. Yet, our analysis suggests that allocations to gold in these commodity indices remain below their optimal weight²⁸

Chart 15: Gold has outperformed all broad-based indices and their individual commodity components

Average annual returns of commodity indices and key individual commodities over the past 20 years*



*Annualised average returns from 31 December 2000 to 31 December 2020. Computations in pound sterling of total return indices for S&P GSCI Agriculture Official Close Index, Bloomberg Commodity Index, S&P GSCI Copper Official Close Index, S&P GSCI Grains Official Close Index, LBMA Silver Price, S&P GSCI Livestock, S&P GSCI Platinum Index, S&P GSCI Total Return CME, LBMA Gold Price PM.

Source: Bloomberg, World Gold Council

26 See: *Gold: the most effective commodity investment*, and *Gold: metal by design, currency by nature*, Gold Investor, Volume 6, June 2014.

27 For more information on the gold weight increases see: *Major commodity indices will increase gold weightings for a second year in a row*.

28 *Gold: the most effective commodity investment*, September 2019.

Focus 2: Gold as an ESG investment

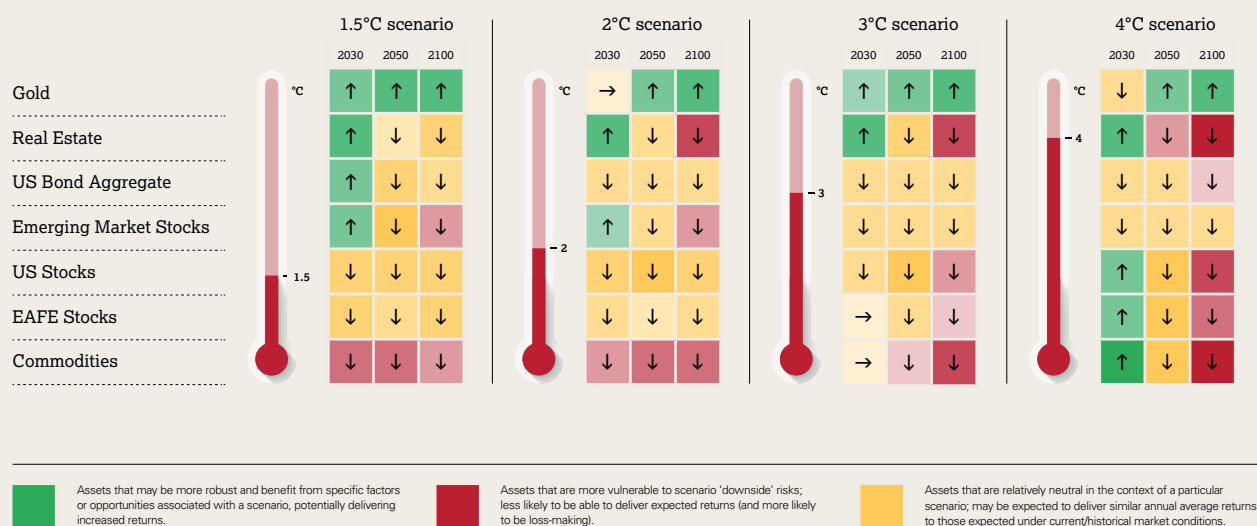
We believe that gold should be considered an ESG-compliant asset. While gold mining is an extractive industry with an impact on the environment, responsible gold miners mitigate risks and contribute heavily to the communities and host countries they operate in, through the likes of direct investments, improvements to infrastructure, access to healthcare and schooling, and much more.

This is demonstrated through the gold mining industry's contribution to the UN Sustainable Development Goals. Our members are committed to the Responsible Gold Mining Principles (RGMPs), launched by the World Gold Council in 2019. The RGMPs are an ambitious set of 51 individual principles that cover all material aspects of ESG related to gold mining and set clear expectations for the entire gold mining industry. Conformance with these Principles will need to be publicly disclosed, with third-party assurance on this disclosure.

In addition, we believe gold can play an important role as a climate-risk mitigating asset within an investment portfolio. Analysis suggests that gold's long-term returns may be more robust than those of many mainstream asset classes in the context of a range of climate scenarios and possible impacts.

Gold may lower the carbon footprint of an investment portfolio over time, as carbon emissions associated with holding physical gold are minimal. Our research indicates that nearly all of the greenhouse gas emissions associated with gold occur during the mining and milling process, primarily from electricity generation and consumption. This makes opportunities to decarbonise gold increasingly accessible and cost-effective, and significant progress is already being made in reducing emissions from mine production.²⁹

Sensitivity of annual returns



²⁹ The Greenhouse Gas Protocol, *Ecoinvent database*. Please see *Gold and climate change: Current and future impacts* and *Gold and climate change: An introduction*. *Gold and climate change: The energy transition*.

The strategic case for gold in the UK

Portfolio construction issues remain

Since the Global Financial Crisis, UK investors have had to adapt to managing their portfolios in a high-risk, high-uncertainty environment. This has led to a renewed focus on robust risk management, to ensure that wealth is protected as well as increased. As the new decade progresses, investors face an expanding set of challenges to asset management and portfolio construction.³⁰

Brexit

The agreement of a trade deal between the UK and the European Union in December 2020 gave welcome relief to many investors. It helped lift some of the uncertainty caused by the UK's 2016 decision to leave the EU, but not all. Further uncertainty lies ahead as the country begins a new era operating independently. New restrictions may mean UK investors face challenges such as reduced liquidity and greater costs, especially those who invest in European assets. Beyond this, a wider set of global risks remain. The deterioration of relations between the US and China, as well as greater levels of protectionism and increased trade tensions, present a significant threat to global demand.

Persistent ultra-low interest rates

As in many other countries, UK investors have endured low and negative interest rates since the global financial crisis. The COVID-19 pandemic has prolonged this trend as policymakers keep rates low to support economic growth. But low interest rates can encourage investors to seek riskier assets to achieve higher returns. Persistently low interest rates also reduce the opportunity cost of holding gold and highlight its attributes as a source of genuine, long-term returns – particularly when compared to historically high levels of global negative-yielding debt – as well as providing much needed diversification.

And a prolonged period of loose monetary policy could also have unintended consequences on asset performance and distort asset allocations for years to come. Additionally, widespread fiscal stimuli and ballooning government debt are raising concerns of potential long-term inflation growth.

Brexit and ultra-low rates continue to support the case for gold in UK portfolios

ESG considerations

Environmental, social and governance (ESG) issues are now decisive in shaping asset selection and strategies. Not only is this in line with wider societal expectations but it is also driven by a host of legal and regulatory changes. A series of co-ordinated statements from the UK government and regulatory authorities (such as the FCA and the Bank of England) in November 2020 confirmed the direction of travel regarding the country's sustainable finance regulations, and added further momentum to moves to clarify the strategies and disclosures of asset managers, life insurers and pension providers in relation to climate-related risks and impacts.³¹

The shift towards greater understanding of this wider set of risks and action to mitigate their negative impacts, has also been a key factor in shaping both the evolution of the gold supply chain and gold's developing role as a climate-change risk-mitigation asset.³²

The role of gold

We believe UK institutional investors stand to benefit from allocating a proportion of their portfolio to gold. In today's environment, we believe that gold has an increasingly relevant role to play in helping UK investors tackle the risk and uncertainty that lies ahead.

³⁰ See 2021 Gold Outlook, January 2021

³¹ World Trade Statistical Review 2019, World Trade Organisation

³² As of 30 September 2020.

European investment demand growth

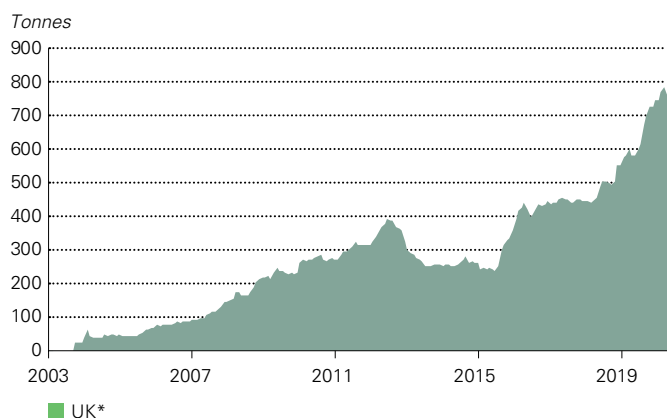
Since the start of 2016, assets in European gold-backed exchange traded products (ETPs) have grown rapidly, hitting a record high of 1,627.1t (US\$98bn) in October 2020. Now accounting for 42% of the global gold-backed ETP market, they have transformed gold investment in Europe. This figure summarises the growth in AUM since 2016, the factors behind it, and the outlook for European gold-backed ETPs.

UK listed gold-backed ETP holdings have grown from 13% to 20% of the global market over the past 10 years, representing an increase of 463 tonnes or £25 billion.

For more information on the European ETP market please see [Market Update: European ETPs reach record highs, April 2019](#).

Chart 16: UK-listed gold backed ETF holdings have doubled in the past few years

Total holdings of UK-listed gold-ETFs



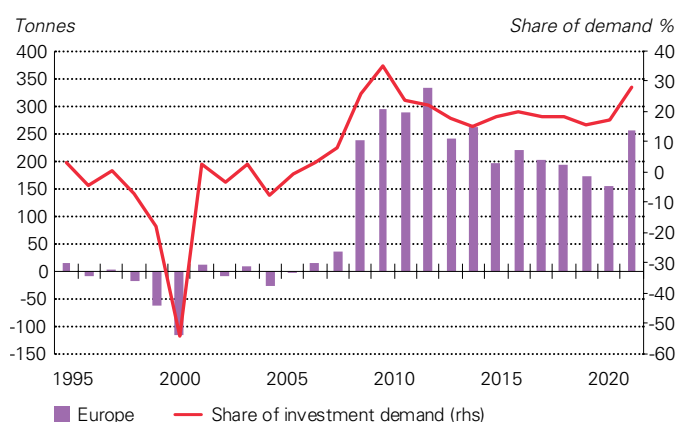
*As of 31 December 2020

Source: Bloomberg, Company Filings, World Gold Council

2020 European bar and coin demand represented the highest percentage of world total demand in over a decade.

Chart 17: European bar and coin demand had its highest percentage of the world total demand since 2009 at 29%

Total bar and coin demand in Europe, compared to the rest of the world



*As of 31 December 2020

Source: World Gold Council

Appendix I: Composition and trends of gold demand and supply

A large yet scarce market

The gold market has two attractive features for investors. Gold's scarcity supports its long-term appeal. But gold's market size is large enough to make it relevant for a wide variety of institutional investors – including central banks.

There are approximately 201,296t of gold above ground, worth more than £9.0trn (**Chart 18**).³³

Mine production has added approximately 3,300t per year over the past decade, equivalent to an annual 1.8% increment of above-ground stocks.³⁴ Mine production is also well diversified across regions (**Chart 19**).

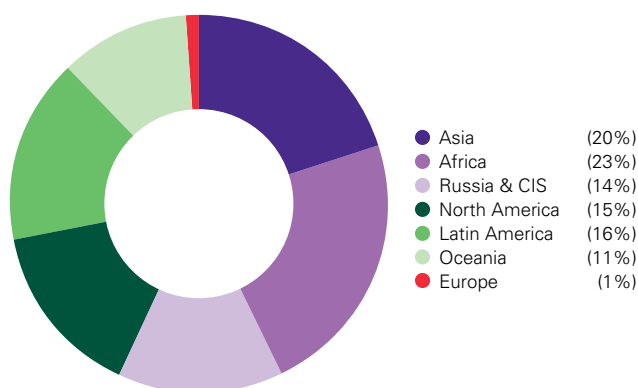
The approximate breakdown of above-ground stocks of physical gold,³⁵ based on its use, is:

- Jewellery: 93,253t (£4.2trn) 46%
- Official sector: 34,211t (£1.5trn) 17%
- Bars and coins: 40,621t (£1.8trn) 20%
- ETFs and similar: 3,764t (£0.2trn) 2%
- Other and unaccounted: 29,448t (£1.3trn) 15%

The financial gold market is made up of bars, coins, gold-backed ETFs and central bank reserves. This segment of the gold market compares favourably to the size of major financial markets (**Chart 18**).

Chart 19: Fewer supply shocks reduce gold's volatility

Gold supply is a mix of mined (72%) and recycled gold (28%); mine production is spread across continents, contributing to gold's low volatility relative to commodities

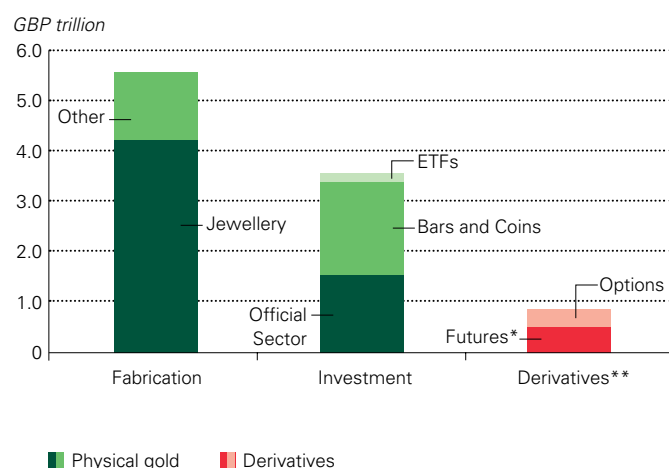


*Computed using average annual supply from 2010 to 2019. Regional breakdown excludes central bank demand due to data availability.

Source: On Goldhub.com: **Gold mine production**.

Chart 18: The size of the financial gold market is large compared to many global assets, and dwarfs known open interest in gold derivatives*

(a) Value of above-ground gold and gold derivatives



* As of 31 December 2020.

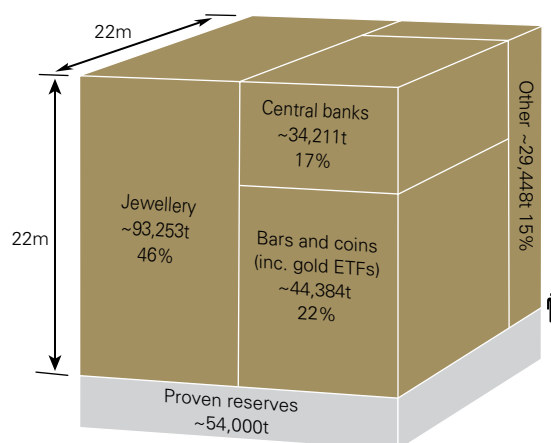
** Represents open interest in COMEX, TOCOM and OTC transactions.

*** Based on 2020 above ground estimates and the standard Olympic swimming pool dimensions of (length = 50m, width = 25m, depth = 2.75m). Includes "other fabrication" (13%) and "unaccounted for" (2%).

On Goldhub.com see: **Financial market size**.

Source: Refinitiv GFMS, Metals Focus, US Geological Survey, Bank for International Settlements; Bloomberg, ETF company filings, ICE Benchmark Administration, Metals Focus, World Gold Council

(b) Total gold supply can fit in just under three Olympic size swimming pools***



33 Based on the 31 December 2020 LBMA Gold Price and 2020 above-ground estimates by Metals Focus, Refinitiv GFMS and the World Gold Council.

34 Based on Metals Focus and Refinitiv GFMS 10-year mine production average as a percentage of above ground stocks, as of 31 December 2020.

35 Ibid footnote 33.

Demand diversity underpins gold's low correlations

Chart 20(a): Gold is bought around the world for multiple purposes – as a luxury good, a component in high-end electronics, a safe-haven investment, or a portfolio diversifier*

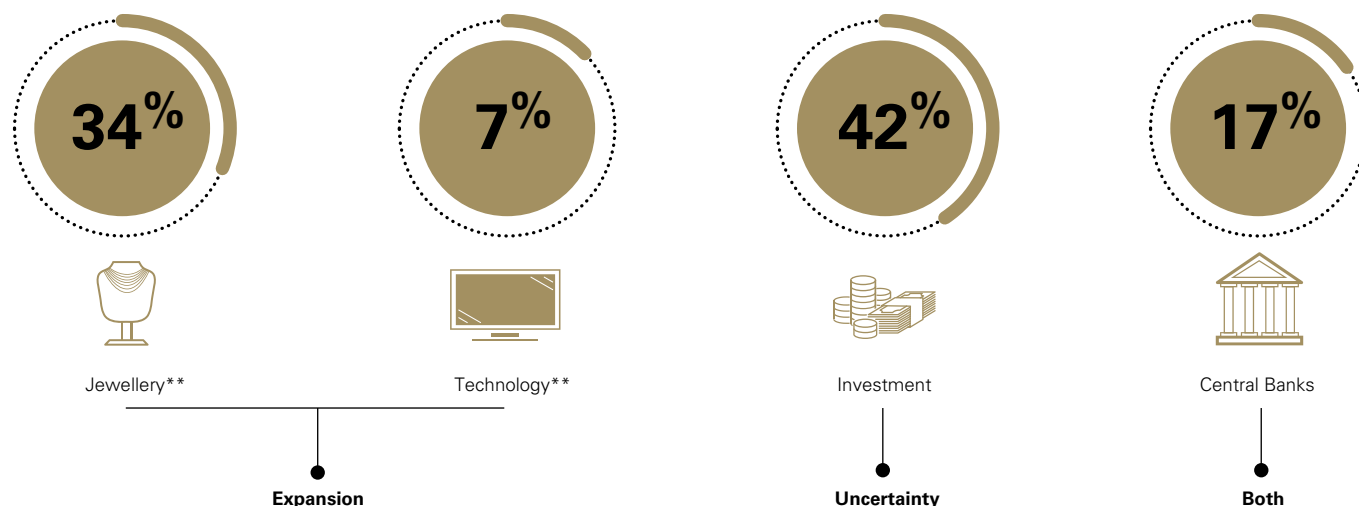
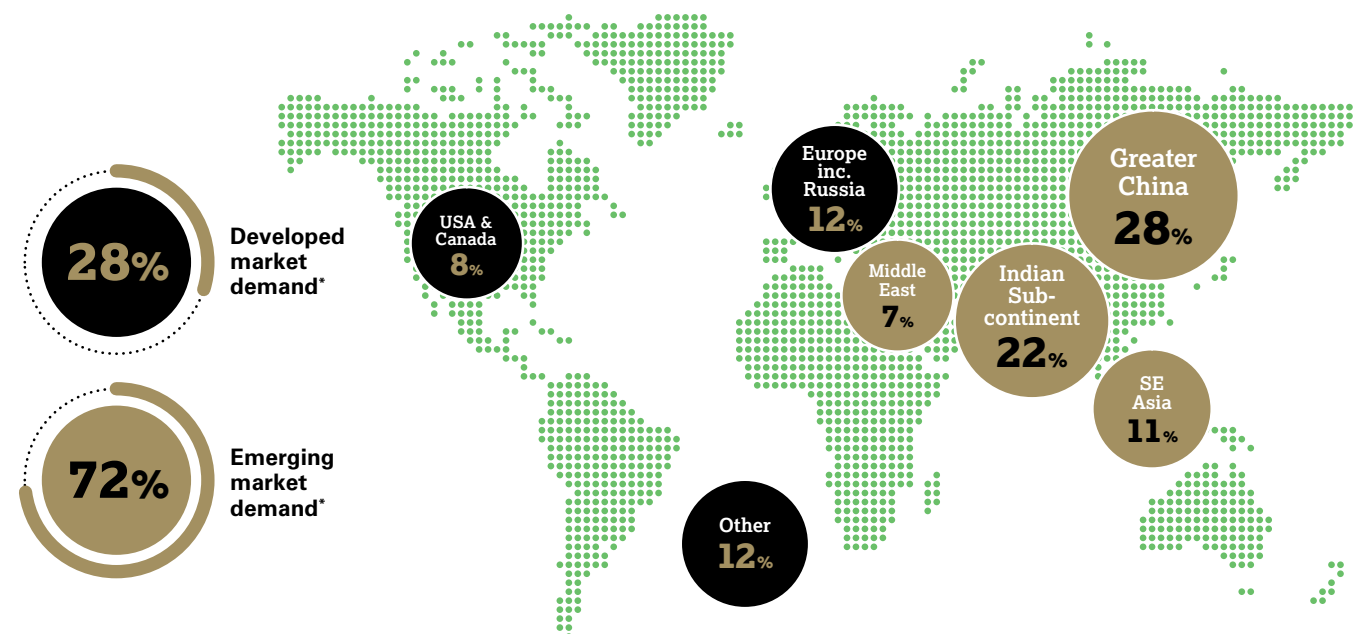


Chart 20(b): Gold demand is geographically diverse, but 72% comes from emerging markets, with China and India representing 50% of all demand.*



* Computed using 10-year average annual demand from 2011 to 2020. Regional breakdown excludes central bank demand due to data availability. Includes: jewellery and technology net of recycling, in addition to bars and coins, ETFs and central bank demand which are historically reported on a net basis. It excludes OTC demand. Figures may not add up to 100% due to rounding.

** Net jewellery and technology demand computed assuming 90% of annual recycling comes from jewellery and 10% from technology.

Source: Bloomberg, Company Filings, ICE Benchmark Administration, Metals Focus, Refinitiv GFMS, World Gold Council

Major trends have reshaped gold demand

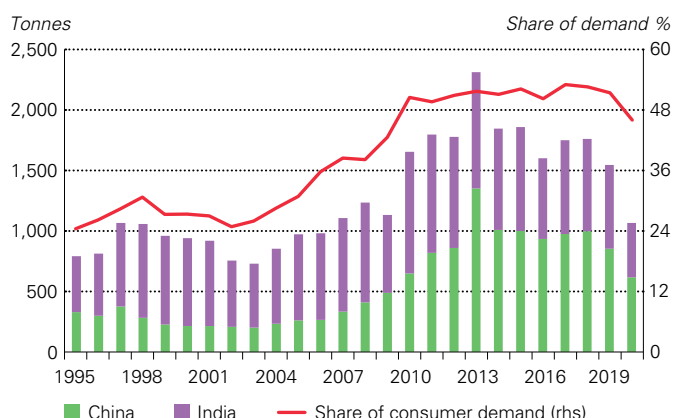
Consumer demand is fuelled by transformational economic growth in China and India. In the early 1990s China and India accounted for 25% of global gold demand. Today, increased wealth has boosted their combined share to nearly 50% (**Chart 21**).³⁶ Expansion of wealth is one of the most important drivers of gold demand over the long run, fuelling jewellery consumption, investment in technology and the acquisition of gold bars and coins.³⁷

Among institutional and retail investors the **introduction of gold-backed ETFs** and similar products has had a material impact on the demand for and exposure to gold. By the end of 2020, gold ETFs had amassed approximately 3,752t of gold, worth £168bn, since they were first launched in 2003 (**Chart 22**).³⁸ The recent growth is particularly pronounced in Europe, where market share has neared levels on par with North America, a sign of global acceptance. Additionally, gold ETFs have become a larger component of overall investment demand (see: **Global gold ETFs: A popular gateway to the gold market**).

Central bank demand transformed in recent years. Reserve managers have been net buyers of gold since 2010 and, more recently, they have purchased multi-decade record amounts of gold, using the asset to diversify their foreign reserves (**Chart 23**).

Chart 21: India and China have doubled their gold market share in less than two decades

Emerging market economic development has created consumer demand and increased market share in India and China*



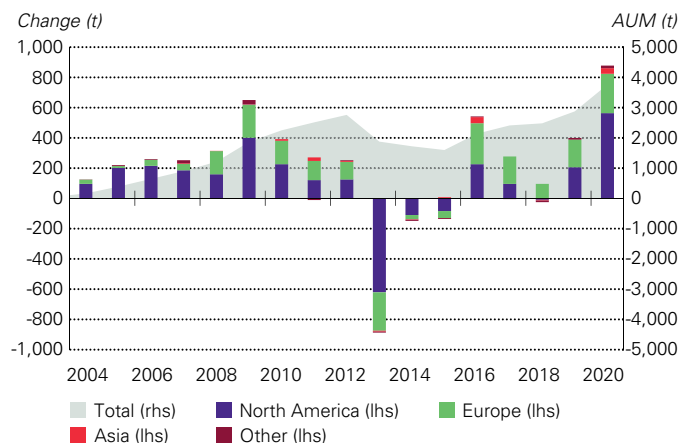
*As of 31 December 2020. Consumer demand is defined as the sum of jewellery, bar and coin demand.

On Goldhub.com see: **Gold Demand Trends**.

Source: Metals Focus, Refinitiv GFMS, World Gold Council

Chart 22: Gold-backed ETFs have introduced new investors to gold across the world

Annual ETF gold demand and cumulative holdings*



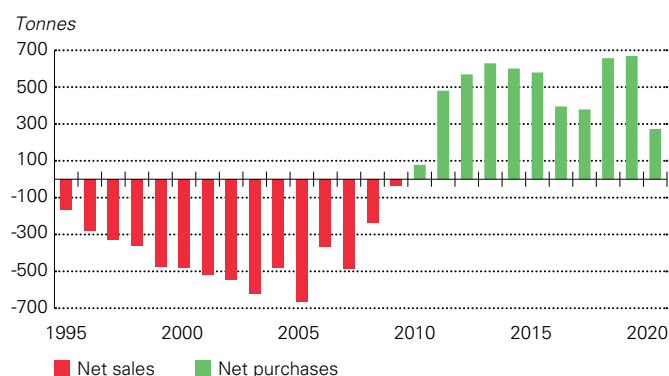
*As of 31 December 2020. Includes gold-backed ETFs and similar products.

On Goldhub.com see: **Global gold-backed ETF holdings and flows**.

Source: Bloomberg, Company Filings, World Gold Council

Chart 23: Central banks have been a steady net source of demand since 2010, led by emerging markets

Net global central bank gold demand*



*As of 31 December 2020

On Goldhub.com see: **Monthly central bank statistics**

Source: Metals Focus, Refinitiv GFMS, World Gold Council

36 As of 31 December 2020.

37 Ibid.

38 As of 31 December 2020.

Appendix II:

Long-term gold performance

Chart 24: Gold returns have been on par with equities and above bonds since the end of the gold standard
Compounded annual growth rate (CAGR) and average annual returns for major asset classes*



* Data from 1 January 1971 to 31 December 2020. Computations in British pound Spot of total return indices for 'Gold': LBMA Gold Price PM GBP, 'Cash': Barclays Benchmark Overnight GBP Cash Index, 'Global bonds': Bloomberg Barclays Global-Aggregate Total Return Index Value Unhedged USD, 'EM equities': MSCI Daily TR Gross EM USD, 'UK equities': FTSE 100 Total Return Index GBP, 'Commodities': Bloomberg Commodity Index Total Return.
** Emerging market returns based on available data beginning in January 1988.

On Goldhub.com see: [Gold returns](#).

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

Additional reading

We include below a list of publications by the World Gold Council that discuss relevant aspects of gold for investors:

Market and Investment Updates

- *Gold and cryptocurrencies: How gold's role in a portfolio differs from cryptos*, February 2021
- *Gold 2021 outlook*, January 2021
- *Gold and central bank reserve management during the COVID-19 pandemic*, May 2020
- *Gold supply chains show resilience amid disruption*, May 2020
- *Gold, an efficient hedge*, April 2020
- *Global gold-backed ETF holdings and flows*, January 2020
- *It may be time to replace bonds with gold*, October 2019
- *Gold: the most effective commodity investment*, September 2019
- *The impact of monetary policy on gold*, March 2019
- *Cryptocurrencies are no substitute for gold*, January 2019
- *Increased transparency on gold trading*, December 2018

Gold Demand Trends

- *Full year and Q4 2020*, January 2021
- *Third quarter 2020*, October 2020
- *Second quarter 2020*, July 2020
- *First quarter 2020*, April 2020

In-depth reports

- *Gold and climate change: The energy transition*, December 2020
- *Global gold ETFs: A popular gateway to the gold market*, November 2020
- *Gold and climate change: Current and future impacts*, October 2019
- *A Central Banker's Guide to Gold as a Reserve Asset – 2019 edition*, September 2019
- *Gold 2048: the next 30 years for gold*, May 2018
- *Enhancing the performance of alternatives with gold*, February 2018

Gold Investor

- *The role of gold in a volatile world*, August 2020
- *Lombard Odier CIO Viewpoint: The case for holding gold*, August 2020
- *Cash down, gold up: Ken Rogoff on the value of gold on a cashless society*, *Gold Investor*, February 2019
- *The curse of cash and the allure of gold*, February 2019

Primers

- *Central banks*, March 2020
- *China's gold market*, March 2020
- *Gold prices*, May 2018
- *Mine production*, May 2018
- *Gold-backed ETFs*, May 2018
- *Recycling*, May 2018

About the World Gold Council

The World Gold Council is the market development organisation for the gold industry. Our purpose is to stimulate and sustain demand for gold, provide industry leadership, and be the global authority on the gold market.

We develop gold-backed solutions, services and products, based on authoritative market insight and we work with a range of partners to put our ideas into action. As a result, we create structural shifts in demand for gold across key market sectors. We provide insights into the international gold markets, helping people to understand the wealth preservation qualities of gold and its role in meeting the social and environmental needs of society.

Based in the UK, with operations in India, China, Singapore and the USA, the World Gold Council is an association whose members comprise the world's leading and most forward-thinking gold mining companies.

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