

## **Present Role of Gold as Part of the Foreign Reserves of the Deutsche Bundesbank**

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### **I. Preamble**

Thank you very much, Terry. I have to say that Terry is a good swimmer as well: we had a competition once.

**Terence Keeley**

I lost.

**Clemens Werner**

### **II. Introduction**

Thank you very much for giving me the opportunity to present some topics about gold. My presentation will be very short and it has three parts: firstly, I will look at the purpose of holding gold from the point of view of the Deutsche Bundesbank, with a brief look into history and then some words on the storage concept that was announced recently.

### **III. Classical Reasons to Hold Gold**

I have selected six classical reasons to hold foreign reserves; two of them apply best for gold. I will not go into detail on all of them, however. Let us start with precautionary holdings; this means the traditional use of reserves as savings for a potential crisis. There is also confidence; gold can provide a level of confidence to a central bank's balance sheet.

The other classical reasons are well known and apply perhaps more for foreign exchange reserves, like the intervention reason. Holding reserves to cover money in circulation has probably lost relevance slightly. Financing and transactions is another classical motive to hold reserves. Last but not least, the investment purpose, which is important for many central banks, but probably not a self-sufficient motive to hold foreign reserves.

### **IV. Functions and Attributes of Gold**

In particular for gold, we can identify four functions and attributes:

- Universal acceptance – gold is accepted as the ultimate independent means of payment almost everywhere. Gold has no country and no currency risk. Gold has no rating.
- Diversification – gold provides an element of diversification to the foreign reserves of a central bank and for the balance sheet.
- Robustness – compared to other assets, gold is very robust against shocks, so it can be seen as an insurance in case of surprising events.

- Gold allows for the absorption of some volatility in the balance sheet. This is true in the case of the Bundesbank reserve, where we have large unrealised profits which are on the liability side and form a kind of buffer for the profit and loss account.

After Bretton Woods, gold could be seen more as a psychological anchor. The purpose of confidence and psychology are well connected to each other.

I have also added two official statements of the Bundesbank with respect to gold. I take the opportunity just to repeat them here because I think they are still valid:

- ‘Gold constitutes an essential component of the Bundesbank’s reserve assets and meets its needs for security and portfolio diversification.’ This assessment was given at a balance sheet press conference in 2006 and is still true.
- ‘Gold continues to perform an important element of ensuring confidence in the stability of the single currency and remains an important element of global monetary reserves.’

## **V. Eurosystem and Bundesbank Gold Holdings**

Here you see the gold holdings of the Eurosystem and of the Bundesbank. You can see that some central banks within the Eurosystem have sold some gold since 1999 and that the Bundesbank has kept its gold holdings quite stable. In this period of time, there were several attempts and also some pressure for the Bundesbank to sell gold. However, in the end the Bundesbank decided not to sell a significant part of its gold reserves.

In terms of size, the Eurosystem is still a large gold holder with 346 million ounces, which is about 10,800 tonnes of gold. The Bundesbank still has 109 million ounces, which is about 3,391 tonnes of gold.

## **VI. Bundesbank Gold Reserves**

### **1. History**

I do not want to go into detail about the history. I can summarise it by saying the Bundesbank’s gold reserves were acquired with current account surpluses, within the European Payments Union and it also received large portions of gold from the Federal Reserve Bank of New York, from the Bank of England and from the BIS.

Here is another chart showing the size of the Bundesbank’s gold reserves. As you can see, between 1945 and 1950, right after the War, Germany had no gold reserves. After that, within the European Payments Union, German gold reserves increased up until 1971, when the dollar gold standard system broke down. Subsequently, these were treated more like passive holdings. You can see significant changes in 1979, when gold was transferred within a swap to the European Monetary Cooperation Fund in preparation of monetary union in Europe. This was transferred back and immediately after that the other important transaction was the transfer of gold to the ECB in 1999. The ECB received 7.46 million ounces from the Bundesbank and all participating national central banks in 1999.

## **2. Book Value**

Here you see the same position expressed in terms of book value. You can see that in 1999 we switched over to a mark to market valuation in the balance sheet. At the end of 2012, the market value has come down recently, but still you can see the amount of unrealised profit.

## **3. Gold in the Balance Sheet**

Another interesting chart is the share of gold within the Bundesbank's balance sheet. It is interesting that the share has been quite stable. From when we started monetary union and at the end of 2012, the share of gold as part of the total assets of the Bundesbank was the same. At the same time, there was an impressive increase in the total assets of the Bundesbank and of many other central banks in the Eurosystem as well. If we used the consolidated Eurosystem balance sheet, the picture would look almost the same. You can also see the time when the balance sheet started to shrink slowly and the gold position decreased as well.

Looking at this, you can say that gold has done quite a good job as a safe haven asset. It performed quite well during these times of market turbulence and it has also, let us say, a counter-cyclical component, which you can see here.

## **VII. Management of Gold Reserves**

There is no active management of gold reserves, no buying and selling every day. The gold position, as of July 2013, is €109 billion.

The Bundesbank has nine kilograms of unallocated gold, so less than one gold bar unallocated, the rest is stored at several locations; I will come back later to that.

The acquisition costs of the gold position are €73. After 1999, we had another level of acquisition costs that has something to do with the switch to mark to market accounting, but the effective acquisition costs are €73.

We do not do gold deposits currently. We did some gold deposits until 2007 for a very small part of the gold reserves in order to finance some of the storage costs, but there has not been a business case since 2007, as before.

There are some annual sales of gold: five to seven tonnes are sold to the Finance Ministry every year within a coin programme.

Last but not least, the Bundesbank also takes care of storage of the gold.

## **VIII. Storage and Relocation**

Gold is stored only within central banks, but let me first give you some words about the objectives, of which there are three: security, liquidity and cost efficiency. Gold is stored at central banks with high international reputations in countries with democratic structures and with banks having the same or comparable security standards, like our own standards.

Of course, the environment changes and so the concept of storage is reviewed regularly. Some of the most significant changes occurred right after the reunification of Germany, when

the reasons to store gold as far to the west and away from the 'iron curtain' no longer applied. Another event was the European currency; because of this it was no longer necessary to store gold in euro area countries. In the meantime, euro banknotes and coins had, for many years, tied up a large volume of world storage, which has now been opened up.

The Bundesbank has made several relocations of gold in 2000, when large quantities of gold were relocated from London to Frankfurt (around 900 tonnes) and further relocations have been announced recently, which you can see on our website. There will be a relocation of 300 tonnes of gold from New York to Frankfurt and 374 tonnes from Paris to Frankfurt. Within this relocation the London Good Delivery standard should be achieved.

I have a table showing you the gold holdings of the Bundesbank and the location where it is stored. As you can see, currently 1,000 tonnes are stored within Germany. The biggest part of the reserves is stored at the Federal Reserve Bank in New York, the Bank of England and Banque de France. This Bundesbank has made this public in a step towards more transparency within the management of the gold reserves and has also published its new target, where about 50% of gold will be stored in Germany with the remainder staying in New York and London.

## **IX. Conclusion**

I hope I have given you some interesting information about the Bundesbank's gold reserves. Thank you very much for your attention and I hope for an interesting discussion.

### **Terence Keeley**

Thank you very much, Clemens. I suggest you sit down and drink a very large glass of water, because when you see the questions that are being asked of you – in fact, could we have a beer at the front table for Clemens?

Alex Gautier will speak next, from the Banque de France. Like Clemens, Alex comes from the markets operations side and directs these activities for the Banque de France. He has helped manage the Banque de France's gold and foreign exchange reserves as well as the risk department, so he speaks with a great deal of authority. Despite having dual nationality – he also has a US passport which he showed me before this session – he does not speak English. Therefore, you should take your translation phone to your ear or are you going to try to do this in English, Alex? Bon chance.