

Rise Of The Golden Dragon

China close to becoming No.1 producer and consumer of gold

Move over India. There is another huge pool of consumers who have taken a shine to gold. Not only do Chinese consumers now buy gold with as much, if not more gusto than Indians, China is also set to become the world's largest producer of the yellow metal. **Shanoo Bijlani and Regan Luis report.**

China is all set to overtake India as the leading consumer of gold for jewellery fabrication, defying global trends which have seen a slump in almost all the major markets over the past few months. Interestingly, China also seems close to unseating South Africa, Australia and the US to become the world's largest producer of the yellow metal.

Thanks to the liberalisation of the Chinese gold market in 2002, the Chinese have become one of the world's leading consumers of the yellow metal. China's phenomenal gold consumption is also being driven by the country's booming economy, which grew by 9 per cent to \$4.39 trillion in 2008. Rising income levels are also rapidly changing lifestyle patterns. The annual disposable income of urban residents increased 34 per cent to 15,781 renminbi (\$2,311) in 2008,

while that of rural residents grew by 33 per cent to 4,761 renminbi (\$700).

China's gold consumption grew by 16 per cent to 409.3 tonnes in the first six months of 2009. In comparison, India's gold consumption remained stagnant during this period, growing just 1 per cent year-on-year to 557.1 tonnes.

In the second quarter of 2009, China was the only major jewellery consuming nation to import more gold compared with a year earlier. In April to June 2009, China registered a 6 per cent increase in gold jewellery consumption, at 72.5 tonnes, and an 11 per cent jump in overall gold demand, at 89.6 tonnes, according to the Gold Demand Trends report published by the World Gold Council (WGC) in mid August. In comparison, India's second-quarter gold jewellery consumption plunged 31 per cent to 88 tonnes, while its overall

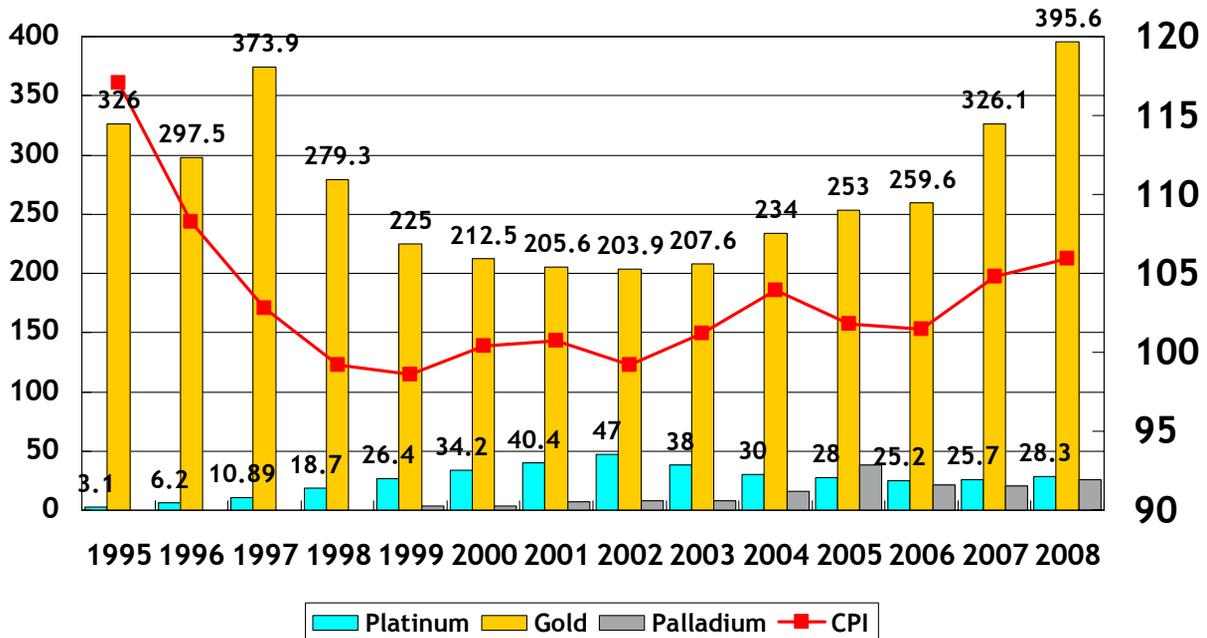


Henry Dunay

China - Total Gold/PT/PD Consumption

Tonnes

CPI



Source: Johnson Matthey and GFMS London



Albert Cheng

gold demand fell by 38 per cent to 109 tonnes.

Albert Cheng, WGC managing director, Far East, elaborated on some of the key jewellery trends in China and gave insights into the reasons behind the increase in gold consumption patterns.

Cheng noted, “The absence of volatility in the local currency against the US dollar helps to explain the resilience in Chinese demand. The renminbi (RMB) gold price has gradually weakened relative to the US dollar price since the beginning of 2008 i.e. the RMB appreciated slightly against the US dollar over that period.

The WGC Gold Demand Trends report added, “The second factor that helps to explain the mystery of China’s resilience in gold demand is the local economy’s ability to withstand the pressures of the global economic downturn. A third factor that we believe contributed to the recent stability in

Chinese gold demand is the absence of a large pool of private ownership – most Chinese consumers are still in the process of accumulating their holdings, despite a long-standing cultural affinity to the precious metal.”

Cheng observed that the recent increase in demand for 24 karat gold jewellery after the current financial crisis reinforced the role of gold as a store of wealth. While the investment motive is strong for buyers of 24 karat gold jewellery, it isn’t as strong for those buying 18 karat gold jewellery, who are seen as individualistic, younger, affluent consumers in major urban centres. This 18 karat consumer bracket had been specifically targeted by the WGC’s advertising campaign titled K Gold.

According to the WGC, the 18 karat jewellery has a greater design element, higher fabrication costs and higher retail mark-up. It is primarily targeted at the more fashion conscious, brand-aware end of the market and

is most popular in the large urban centres, where income growth is most rapid and western styles are making the biggest inroads. A significant proportion of this 18 karat jewellery is imported from Italy.

Despite the growth of the 18 karat jewellery segment, down-karat is not a significant threat in China, the WGC report stated. While the cities are likely to experience a continued trend towards 18 karat jewellery as the population flow from rural regions to cities continues, a strong base in 24 karat jewellery is expected to remain.

Currently, the 24 karat gold market is showing the most resilience, while weaker demand for the 18 karat segment is attributable to a shift in consumer preferences towards platinum, which has benefited from a price fall at the retail level of approximately 40 per cent this year. Notably, the lighter and more design-oriented 24 karat jewellery, which also has a higher cost component and tends to sell by weight, has not suffered the same weakness.

The WGC report notes that the cultural affinity to gold in China may not be quite as strong as it is in India, but gold ownership is nevertheless a key part of the wedding- and gifting seasons and the process of wealth protection and accumulation. "The potential for jewellery demand to grow, we believe, is significant – average per capita off-take via jewellery in China during the five years to December 2008, at just 0.20 grams, was less than half of that in India and just over a fifth of that in the US. The trend for the last five years has been gradually but steadily upward. At the same time, there is also significant potential for new investment in bars and coins," it said.

China Will Inevitably Become A Gold Trading Centre

Albert Cheng, WGC managing director, Far East, shares some of his views with Solitaire.

- **How much has China's annual new gold consumption increased over the last five years?**

China's gold consumption shows a steady growth since 2003 in pace with the GDP growth. (See graph)

- **The jewellery retail industry in India caters to the investment market by also selling medallions (which are called gold 'coins') and investment bars – usually stamped with the retailer's own logo. In the last few years, Indian banks have moved aggressively into this space, with epoxy-sealed bubble packs guaranteeing the purity of the gold. Are there any parallels in China?**

Most of the investment consumption in China is done through epoxy-sealed gold bars in 10-, 50-, 100-, 500 grams and 1 kilo. These are sold either at banks or gold jewellery stores. We do not have a history of selling medallion (or gold coins).

- **How much do you think China's annual gold consumption will be in two to five years?**

I hope it will increase in tandem to the GDP growth or higher.

- **Tell us about China's gold consumption pattern. Is there a major festival season (like Christmas in the West and Diwali in India) when most gold and gold jewellery is bought?**

Gold jewellery is bought all year round, but weddings, by far, are the number one reason for gold jewellery purchases, normally towards the end of the year. Weddings are followed by the Chinese New Year and holidays such as Labour Day in May and National Holiday in early October.

- **Is the WGC targeting any specific gold-buying periods in its China initiatives?**

For pure gold jewellery, we work closely with trade partners during the wedding season and long holidays. However, for K-Gold (18 karat), which is targeted at young people as fashion accessories, we work with trade partners more closely with the changes in seasonal trends, like say, spring and autumn collections.

- **Are there any specific product categories (either in investment or in jewellery) that show the strongest promise in generating sales?**

Mostly investment products are sold through financial institutions or specific bullion houses with very low premium, while jewellery products need to be stylish and of good quality. In the past few years, we were trying very hard to improve both the design and quality with the trade through our promotional programmes.

- **Now that China mines so much gold, do you see the country becoming a major trading centre, the way South Africa is?**

I think this development is inevitable.

- **Do you think China's gold production in combination with its own heavy consumption could set the benchmark for pricing – the way India did for a long time on the strength of its consumption alone?**

Gold price is not going to be set by any particular group of players. The price is based on worldwide demand and supply and nobody can set the price. You can only influence its movement with seasonal demand.

- **Any other observations you might have.**

Both India and China are going to be playing a very important role in the future of the global gold market, because of their size and the wealth that is going to be accumulated going forward.