# Central banks and other institutions

## Uncertainty intensifies as Brexit adds to negative interest rate challenges; central banks continue to seek support in gold.

| Tonnes | Q2'15 | Q2'16 | Year-on-year change | Year-to-date change |
|---|---|---|---|---|
| Central banks and other institutions | 127.3 | 76.9 | ↓ -40% | ↓ -23% |

The second quarter saw central banks purchase – on a net basis – 76.9t. Net purchases year-to-date now total 185.1t. This represents year-on-year declines of 40% (Q2) and 23% (H1) respectively. But these declines have coincided with a 25% rise in gold prices over H1 2016, which has dramatically increased the value of central bank gold holdings. World official gold holdings of over 32,800t at the end of June were equivalent to approximately US$1.4trn – the highest value since Q1 2013, when average gold prices were around 30% higher than average Q2 levels.[18]

Russia (+38.4t), China (+25.9t) and Kazakhstan (+9.8t) remain the dominant driving forces behind this increase in global gold reserves. The quarterly total was impacted by China taking a pause in May, coinciding with a slowing in buying by Russia, before both resumed their recent rates of purchasing in June. Buying by other, predominantly emerging market, central banks were in more limited quantities over the quarter. Conversely, Jordan (-5.6t),[19] Belarus (-2.5t) and Ukraine (-2.2t) were net sellers during the quarter, while Germany sold 2.7t as part of its ongoing coin-minting programme.

The first six months of 2016 proved to be a uniquely challenging time for reserve managers. The unprecedented prevalence of global negative interest rates was compounded in the second quarter of the year by the equally unprecedented uncertainty surrounding Brexit. Continued central bank purchases proved again that reserve managers view gold as such an important reserve asset, especially with respect to portfolio diversification and capital preservation. Such an environment also helps to highlight that gold is a high quality, liquid asset with no intervention risk.

The UK's seismic decision to leave the EU sent shockwaves through financial markets at the end of the quarter. The British pound depreciated to its weakest level against the US dollar in 31 years, while Bank of England governor Mark Carney indicated UK monetary policy could be eased further in the face of a weaker economic outlook. The International Monetary Fund also revised lower its global growth forecast following the vote.[20]

18 IMF data for end-June not available at time of writing. Value calculated using estimated end-June global central bank holdings and end-June gold price.

19 Data for Jordanian gold reserves is only available for May at the time of writing.

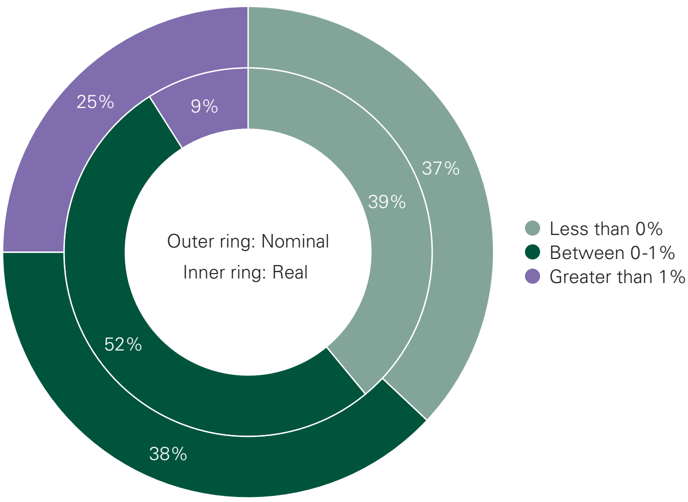
20 International Monetary Fund, *World Economic Outlook Update*, July 2016.

Importantly for reserve managers, the decision also weighed on global sovereign bond yields, further shrinking the pool of investible assets. As discussed in GDT Q1 2016, the shadow of low and negative interest rates continues to hang over central banks (**Chart 9**). At the end of June, Fitch Ratings[21] estimated that the pile of sovereign debt with negative yields has grown to a whopping US$11.7tn – increasing by US$1.3tn since the end of May alone.

Amid this growing prevalence of global negative interest rates, reserve managers are finding they have less room for manoeuvre. And recent currency interventions by the Swiss National Bank, following the Brexit vote, to halt the appreciation of the Swiss franc (considered a safe haven and key reserve currency) have served to compound the issue. Additionally, in mid-July, the Japanese yen – another key reserve currency – saw a steep depreciation against the US dollar after the suggestion of further accommodative monetary policies by the Bank of Japan (specifically the possible introduction of "helicopter money") caused market jitters.

**Chart 9: Advanced Economy Sovereign Debt Outstanding (as of 27 July 2016)**

- Central banks need to cast their net wider in the search for yield in an environment of negative interest rates.
- The UK's Brexit decision compounded uncertainty levels, putting both sterling and the Swiss franc under pressure.




Note: Sovereign debt from Australia, Canada, Denmark, Euro area (investment grade), Japan, Sweden, Switzerland, the United Kingdom and the United States. May not equal 100% due to rounding.

21 https://www.fitchratings.com/site/pressrelease?id=1008156