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Barrick shuts hedge book as world gold supply runs out

Global gold production is in terminal decline despite record prices and Herculean efforts by mining companies to discover fresh sources of ore in remote spots, according to the world's top producer Barrick Gold.

By Ambrose Evans-Pritchard, International Business Editor
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Liquid gold: Gold is poured from the induction kiln Photo: JULIAN SIMMONDS

Aaron Regent, president of the Canadian gold giant, said that global output has been falling by roughly 1m ounces a year since the start of the decade. Total mine supply has dropped by 10pc as ore quality erodes, implying that the roaring bull market of the last eight years may have further to run.

"There is a strong case to be made that we are already at 'peak gold'," he told *The Daily Telegraph* at the RBC's annual gold conference in London.

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"Production peaked around 2000 and it has been in decline ever since, and we forecast that decline to continue. It is increasingly difficult to find ore," he said.

Ore grades have fallen from around 12 grams per tonne in 1950 to nearer 3 grams in the US, Canada, and Australia. South Africa's output has halved since peaking in 1970.

The supply crunch has helped push **gold** to an all-time high, reaching $1,118 an ounce at one stage yesterday. The key driver over recent days has been the move by India's central bank to soak up half of the gold being sold by the International Monetary Fund. It is the latest sign that the rising powers of Asia and the commodity bloc are growing wary of Western paper money and debt.

China has quietly doubled holdings to 1,054 tonnes and is thought to be adding gradually on price dips, creating a market floor. Gold remains a tiny fraction of its $2.3 trillion in foreign reserves.

Gold exchange-traded funds (ETFs) – dubbed the "People's Central Bank" – have accumulated 1,778 tonnes, making them the fifth biggest holder after the US, Germany, France, and Italy.

Ross Norman, director of theBullionDesk.com, said exploration budgets had tripled since the start of the decade with stubbornly disappointing results so far.

Output fell a further 14pc in South Africa last year as companies were forced to dig ever deeper - at greater cost - to replace depleted reserves, not helped by "social uplift" rules and power cuts. Harmony Gold said yesterday that it may close two more mines over coming months due to poor ore grades.

Mr Norman said the "false mine of central banks" had been the only new source of gold supply this decade as they auction off reserves, but they are switching sides to become net buyers.

Barrick is moving fast to wind down the remaining 3m ounces of its infamous hedge book over the next twelve months, an implicit bet on rising gold prices over time.

Mr Regent said the company had waited too long to ditch the policy, which has made the company enemy number one among 'gold bug' enthusiasts. The hedges oblige Barrick to deliver part of its gold into futures contracts set long ago at levels far below today's spot prices.

The strategy worked well in the falling market of the 1990s, but has cost the company dear in lost profits this decade. "Hindsight is always 20/20," said Mr Regent, who was appointed from the outside earlier this year.

Barrick bit the bullet in the third quarter, taking a $5.7bn charge against earnings on hedge contracts. Liberation is at last in sight. In 2001 the hedge book topped 20m ounces.

Mr Regent said the hedge policy has weighed badly on the share price and irked investors, becoming a bone of contention at every meeting. The financial crisis brought matters to a head as markets fretted about counterparty risk. "It was clear to me that there were a significant number of institutions who wouldn't invest in Barrick because of the hedge book," he said.

Barrick produced 1.9m ounces of gold last quarter, down from 1.95m a year earlier. Costs have been "trending down" to $456 an ounce, though rising energy prices pose a fresh threat. Total reserves are 139m ounces, far ahead of rival Newmont Mining at 86m.

The hedge book venture has not been a happy one, but those who predicted that Barrick would eventually "blow up" on its contracts may owe the company an apology.