

# **The role of gold as a strategic asset in Islamic Finance**

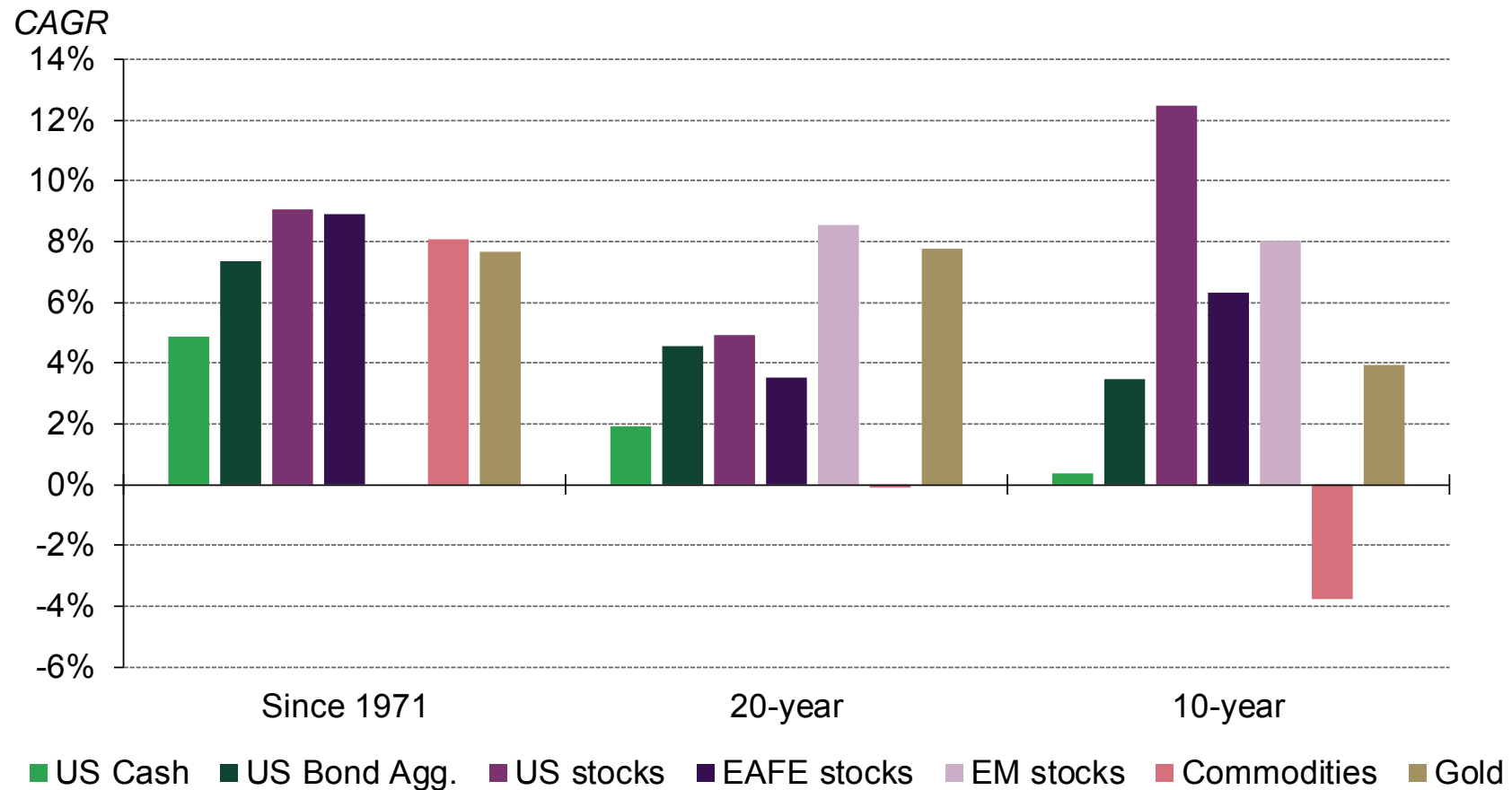
**April 2019**

# Strategic case for gold



# The strategic case for gold: returns

## Gold's long-term performance compared to other financial assets\*

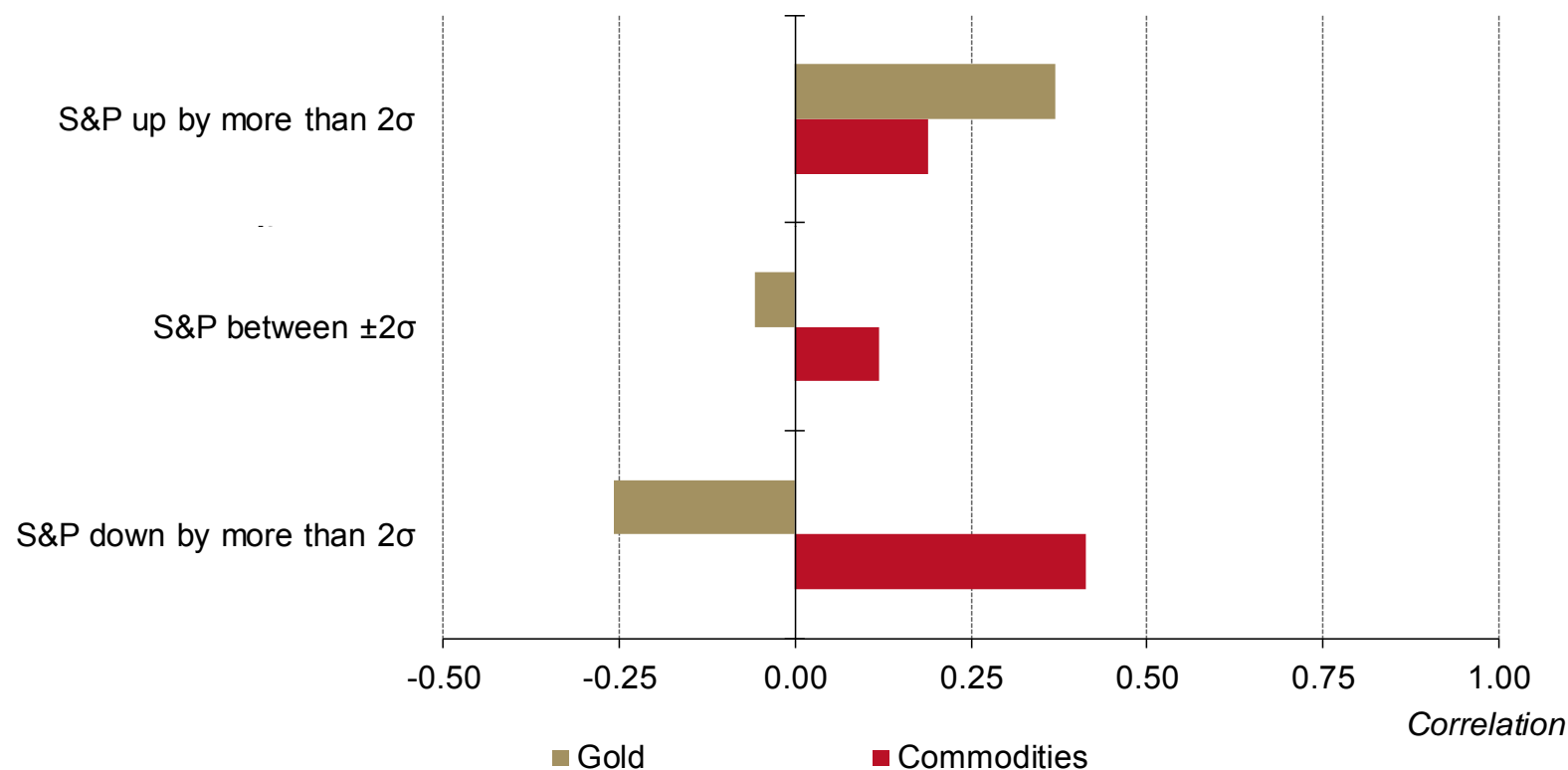


\*As of 31 December 2018. Based on total returns including MSCI US, MSCI EAFE net, MSCI Emerging Markets net, JP Morgan 3-month US cash, Bloomberg Barclays US Bond Aggregate, Bloomberg Commodity Index. Gold performance based on the LBMA Gold Price.

Sources: Bloomberg, ICE Benchmark Administration, World Gold Council

# The strategic case for gold: diversification

## Correlation of US stocks versus gold, commodities\*



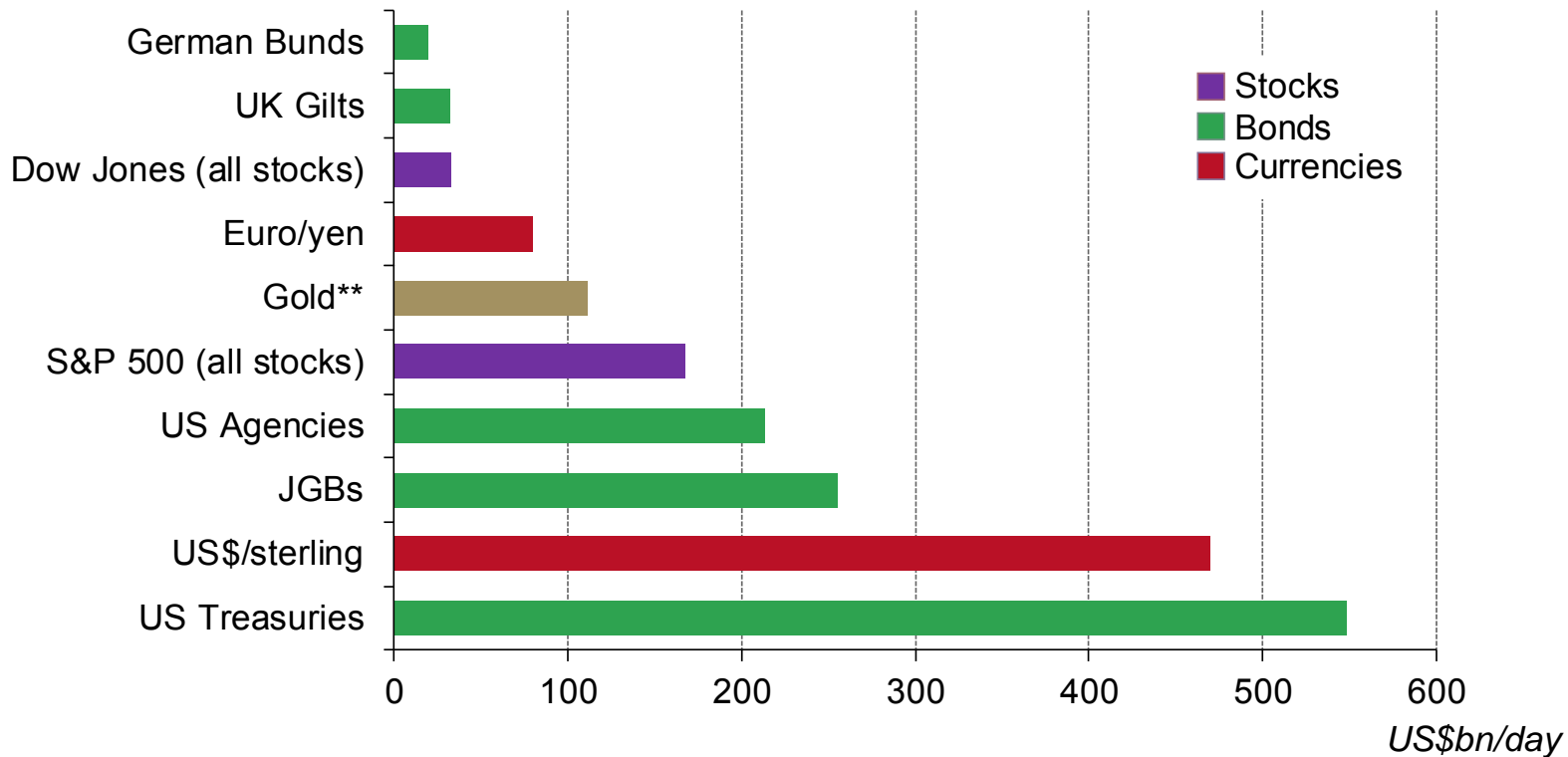
\*Based on weekly returns of the S&P 500, LBMA Gold Price and the S&P Goldman Sachs Commodity Index using data between 1 January 1987 and 31 December 2018.

Sources: Bloomberg, ICE Benchmark Administration, World Gold Council

# The strategic case for gold: liquidity

## Gold trades more than many other major financial assets

Average daily trading volumes in US\$\*



\*Based on estimated 1-year average trading volumes as of 31 December 2018, except for currencies that correspond to 2016 volumes due to data availability.

\*\* Gold liquidity includes estimates on over-the-counter (OTC) transactions, and published statistics on futures exchanges, and gold backed exchange-traded products.

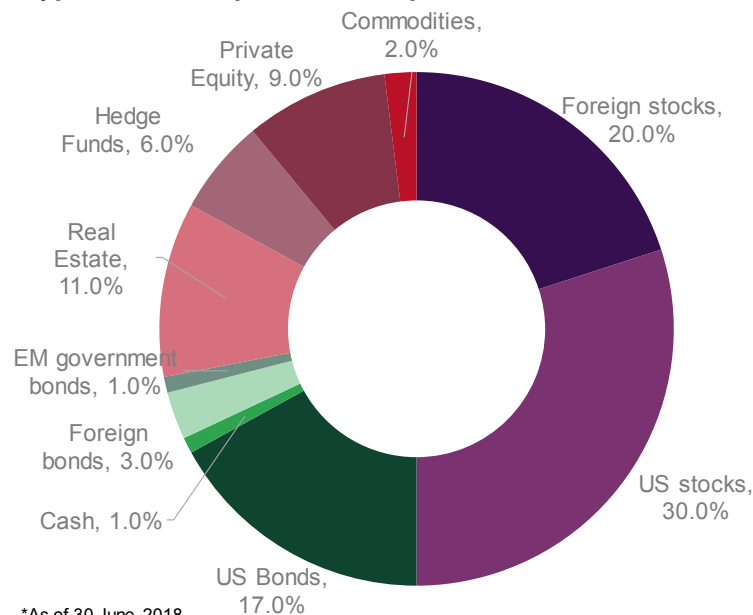
Sources: BIS, Bloomberg, German Finance Agency, Japan Securities Dealers Association, LBMA, UK Debt Management Office, World Gold Council

# The strategic case for gold: portfolio impact

10-year analysis of a hypothetical pension fund portfolio

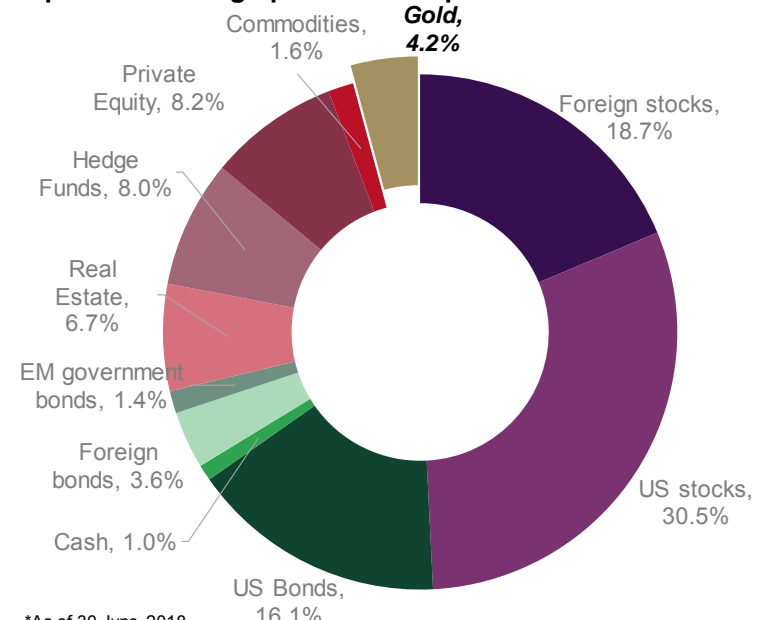
5.6%	<b>Return</b>	5.7% ↑
13.1%	<b>Volatility</b>	12.1% ↓
-43.5%	<b>Max Drawdown</b>	-38.9% ↓

**Hypothetical US pension fund portfolio\***



\*As of 30 June 2018.  
Based on the 2018 Global Pension Fund Asset Study and 2017 Global Alternatives Survey.  
Source: Willis Towers Watson, Bloomberg, World Gold Council

**Optimized average pension fund portfolio\***



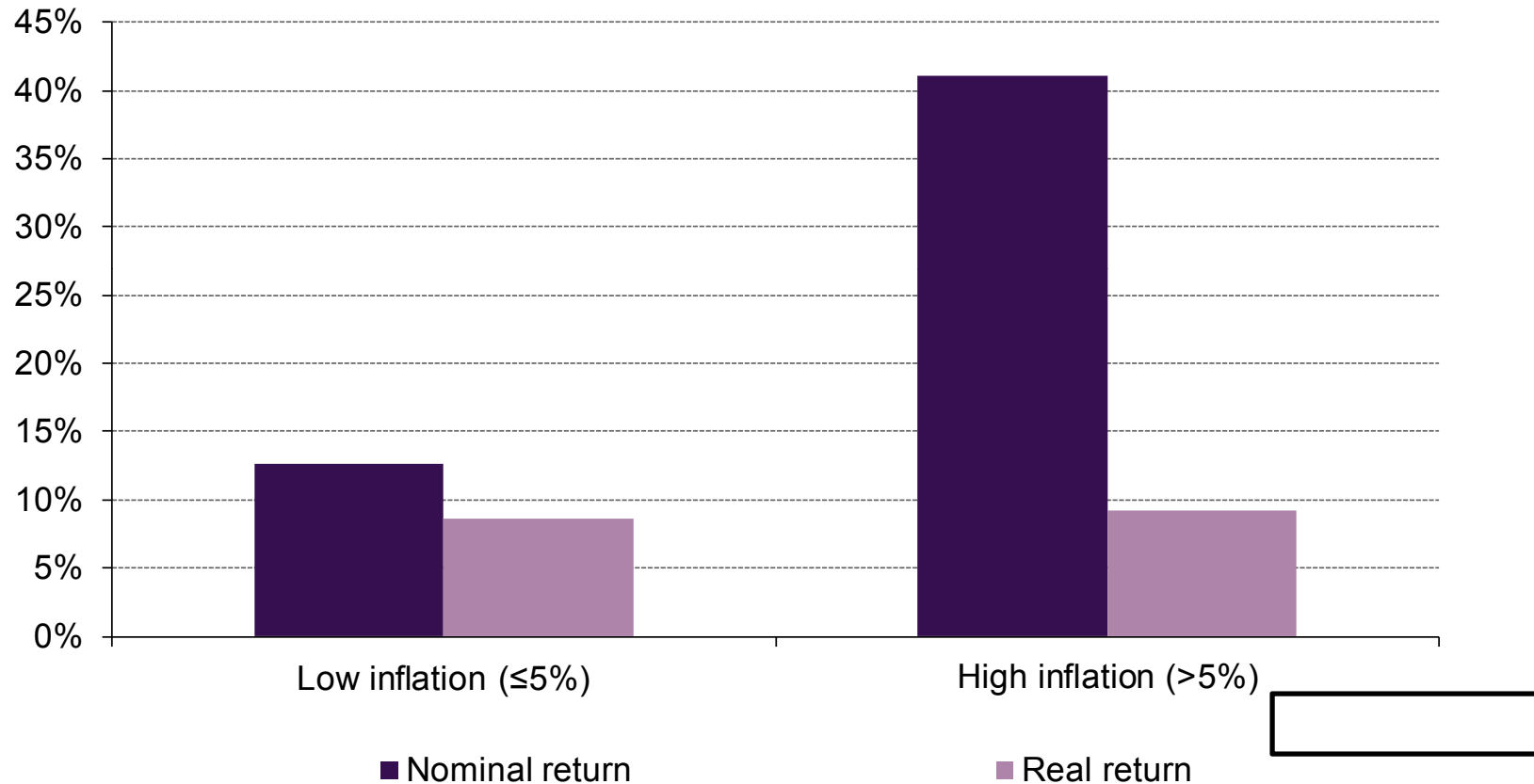
\*As of 30 June 2018.  
Based on re-sampled efficient optimization.  
Source: Willis Towers Watson, Bloomberg, World Gold Council

\*Willis Towers Watson provides analysis of typical portfolio allocations of global pension funds as of December 2018

# Gold and capital preservation: inflation

## Gold returns as a function of annual inflation\*

*Avg. annual return*



\*Inflation computed using annual CPI year-on-year changes between 1971 and 2018.

\*\* For each year on the sample, real return =  $(1 + \text{nominal return}) / (1 + \text{inflation}) - 1$ .

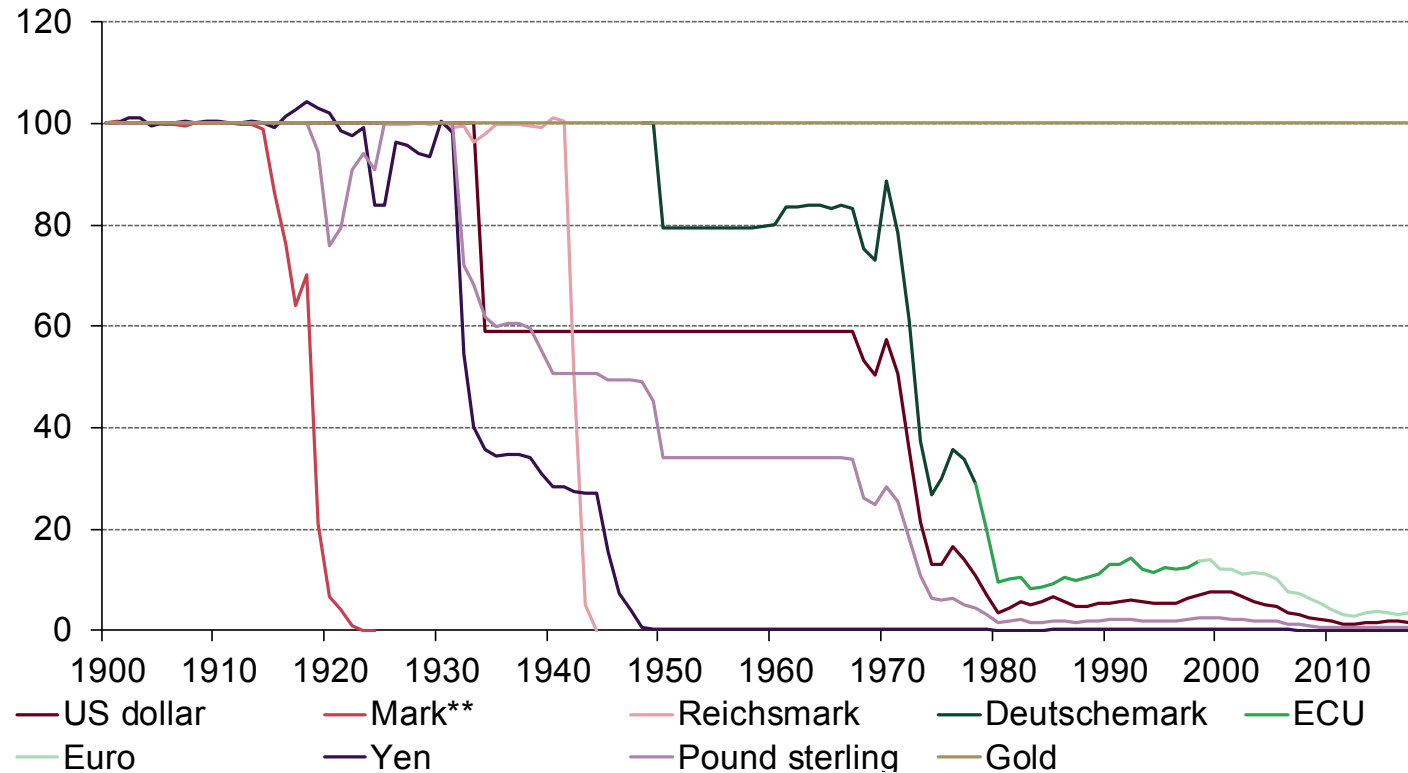
Sources: Bloomberg, ICE Benchmark Administration, World Gold Council

# Gold and capital preservation: currency

## Gold and currency depreciation

### Relative value between major currencies and gold since 1900\*

*Value relative to gold (1900=100)*



\*As of 31 December 2018. Based on the annual average price of a currency relative to the gold price.

\*\* The “Mark” was the currency of the late German Empire. It was originally known as the Goldmark and backed by gold until 2914. It was known as the Papermark thereafter.

Sources: Bloomberg, Harold Marc use – UC Santa Barbara, World Gold Council



# Gold in Islamic Finance

# AAOIFI Shari'ah Standard on Gold

The AAOIFI Shari'ah Standard clarifies the Shari'ah treatment of gold trading and investing. It was launched at the World Islamic Banking Conference in 2016.

A dedicated website ([www.shariahgold.com](http://www.shariahgold.com)) hosts the Standard and related materials.



# Key principles

1. Gold must be **traded on a spot basis** (hand-to-hand). Conventional forwards and futures are not permissible.
2. Gold can be **owned on a physical or a constructive basis**. This very important as it allows gold products to be structured.
3. In the case of constructive possession, **gold has to be fully allocated**. Unallocated gold is not permissible.
4. Allocation can occur through either T+0 settlement OR the receipt of a certificate/email **specifying bar ownership**.
5. It is **permissible to own gold jointly**, where each partner owns an undivided beneficial interest in a trust. This is important for structuring purposes, such as for some physical gold ETFs.

# Industry reaction

*“AAOIFI’s Shari’ah expertise and the World Gold Council’s industry know-how have ensured that the Standard becomes the basis not only for the inclusion of a historically and economically important asset class, but for the stability of Islamic Financial Institutions around the world.”*

**Sheikh Yusuf DeLorenzo**  
International Shari’ah Scholar and advisor to Dow Jones

*“There is a recent precedent that initially contradictory opinions can converge and finally allow a collective fatwa – namely, the AAOIFI Shari’ah Standard 57 on gold and its Trading”*

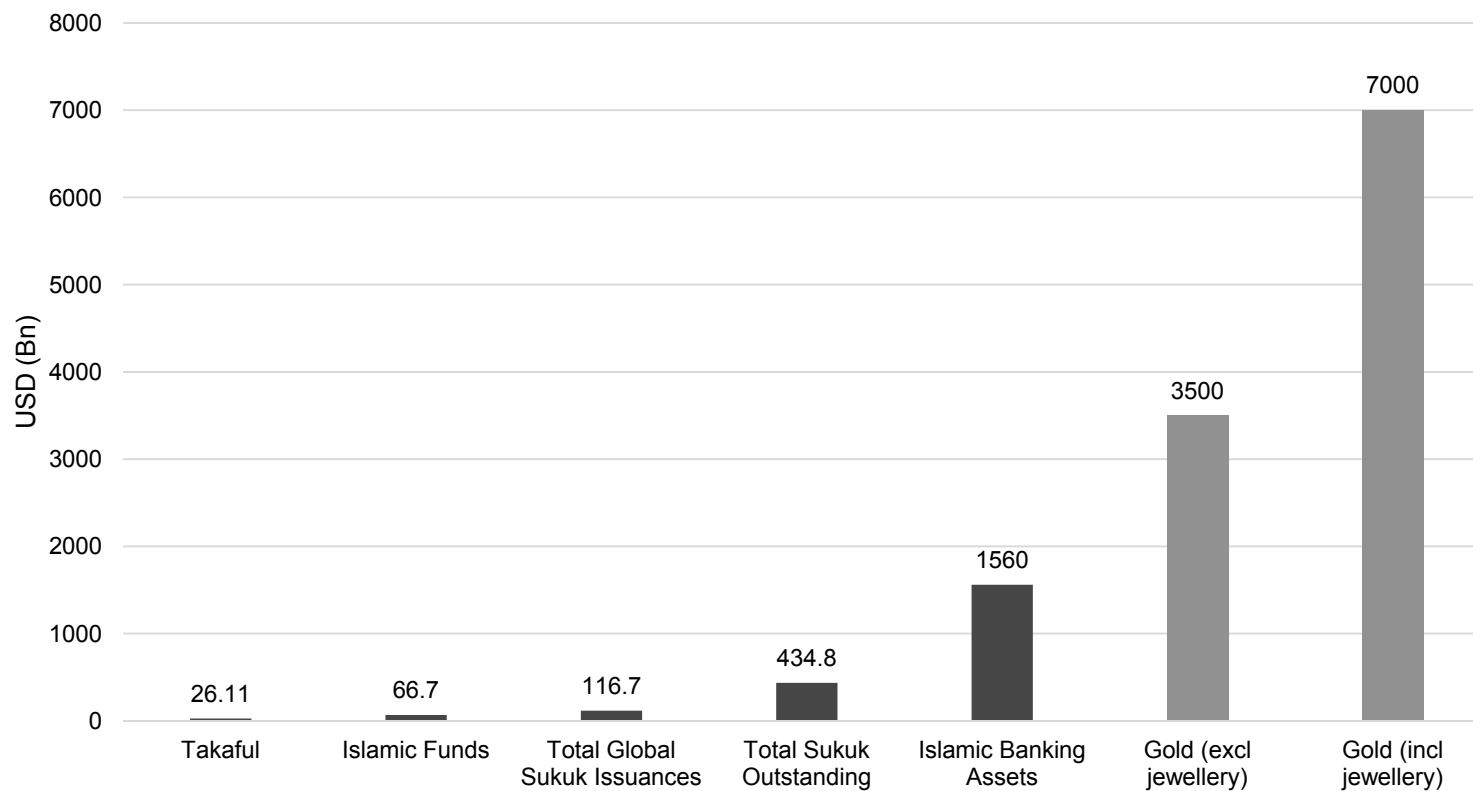
**Islamic Financial Services Board (2017 Financial Stability Report)**

*"Given its history and reputation, the opportunity for the use of gold in Islamic finance is clear... This Standard will enable the foundation of what could be the most significant event for Shari’ah finance in modern times."*

**Dr Mark Mobius**  
former Chairman, Templeton Emerging Market Fund

# The gold market is large and liquid

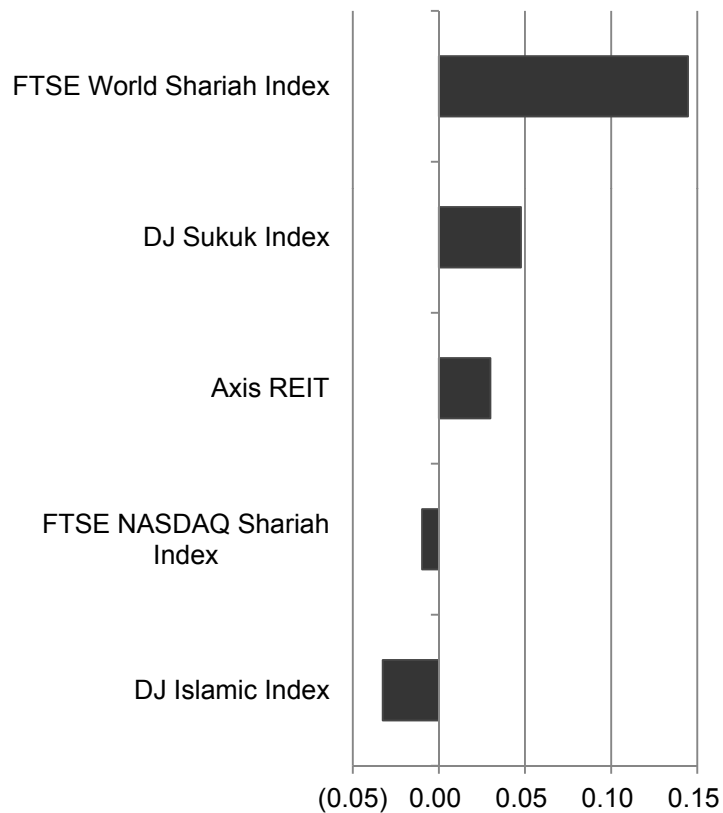
The gold market is larger and more liquid than major Islamic asset classes



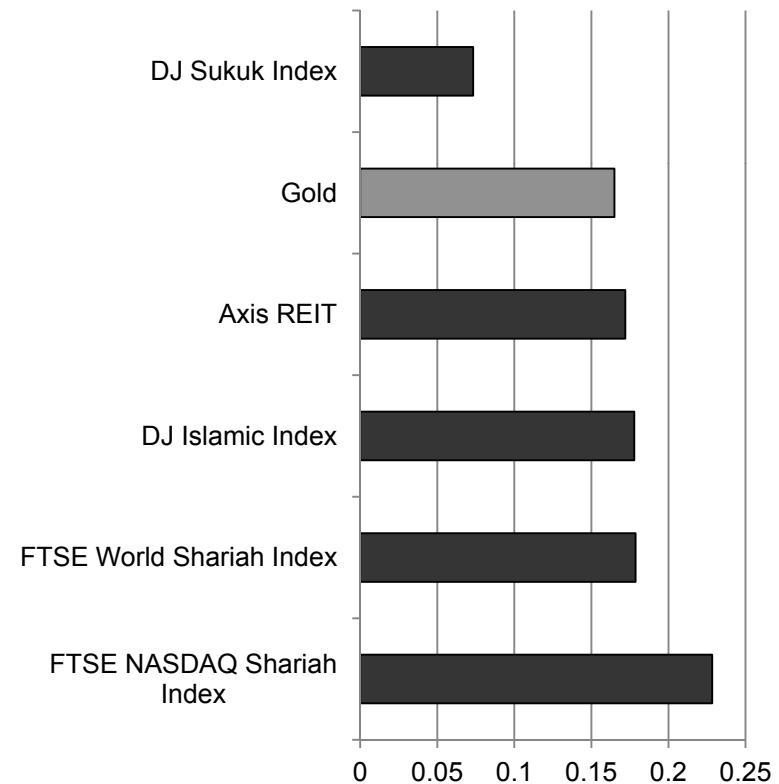
Sources: IFSB, IIFM, World Gold Council. As at end 2017 except Sukuk issuances (2016)

# Gold is a powerful diversifier

**Islamic Asset Classes  
Correlation to Gold (10 Year)**

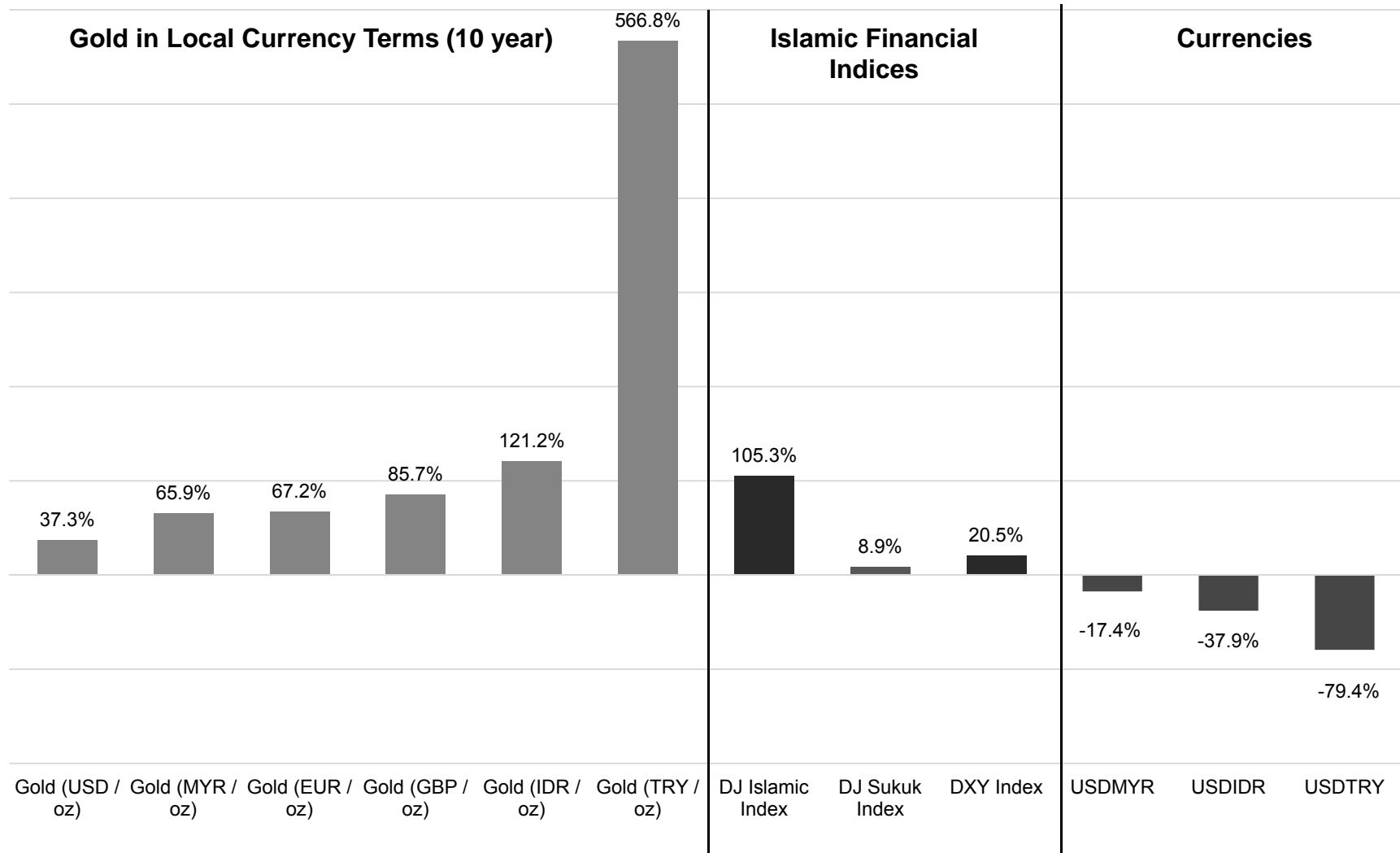


**Annualized Volatility of Islamic  
Assets and Gold (10 Year)**



Source: World Gold Council; Bloomberg. As of 8 Oct 2018

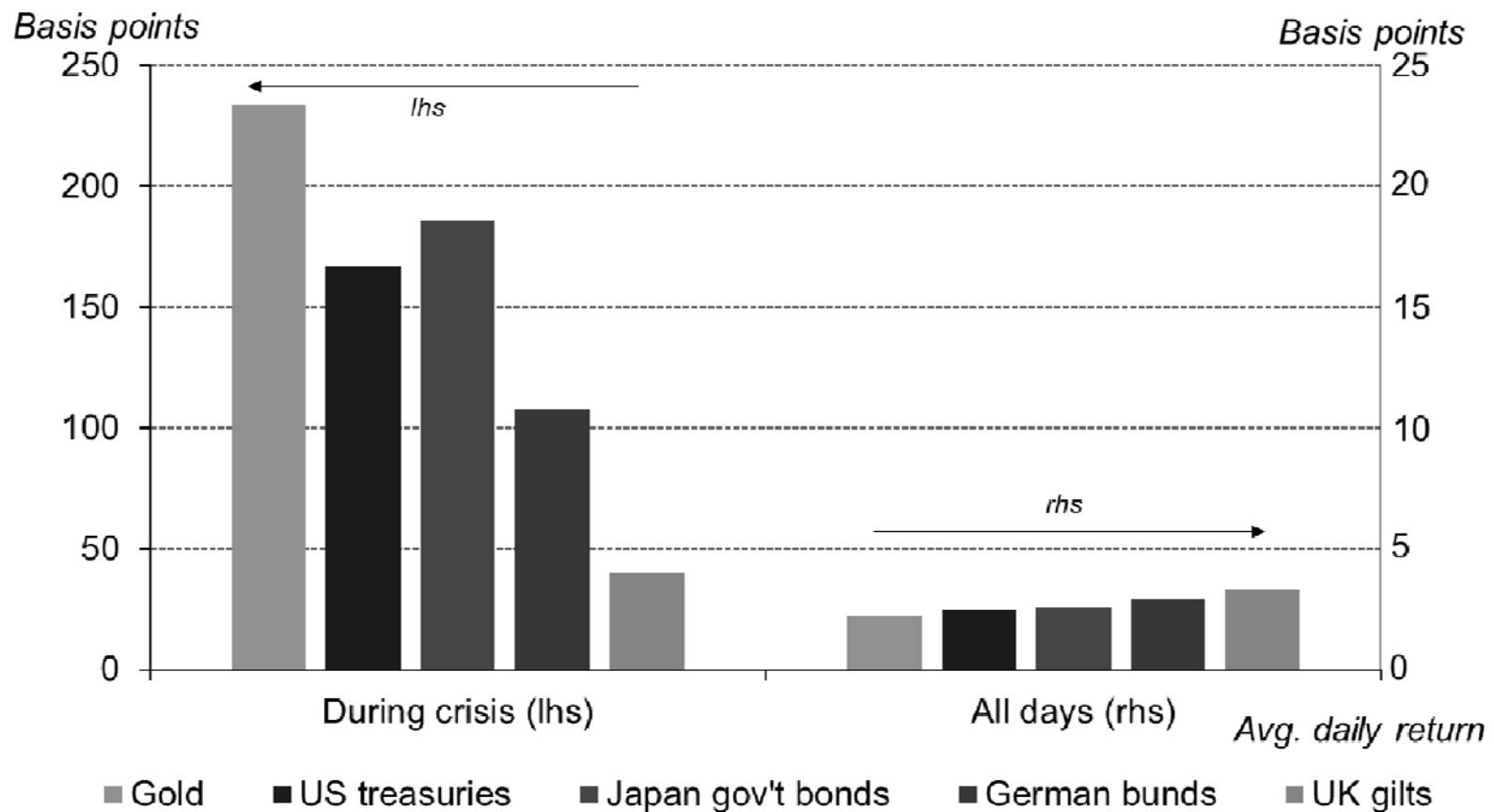
# Gold outperforms other Islamic asset classes



Sources: World Gold Council; Bloomberg. As of 8 October 2018

# Gold is a Shari'ah-compliant safe haven asset

**Financial asset performance during times of crisis\***



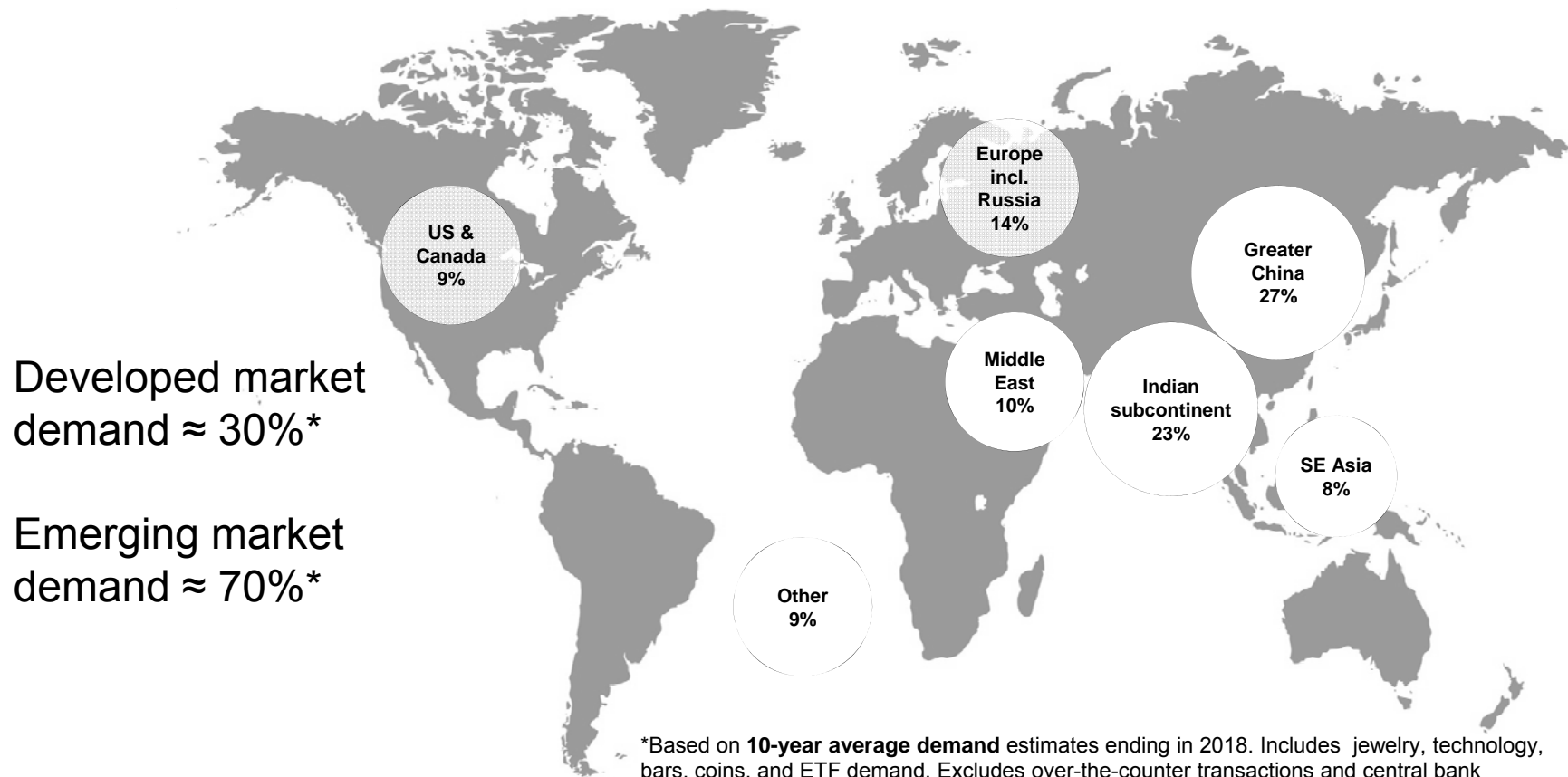
\*Crises include: Black Monday (1987), LTCM (1998), Dot-com bubble (2000-2001), September 11<sup>th</sup> (2001), recession (2002), financial crisis (2007 – 2009), sovereign debt crisis I (2010), sovereign debt crisis II (2011)

Sources: Bloomberg, NBER, World Gold Council



# Annex

# Gold is a global market



Developed market  
demand  $\approx$  30%\*

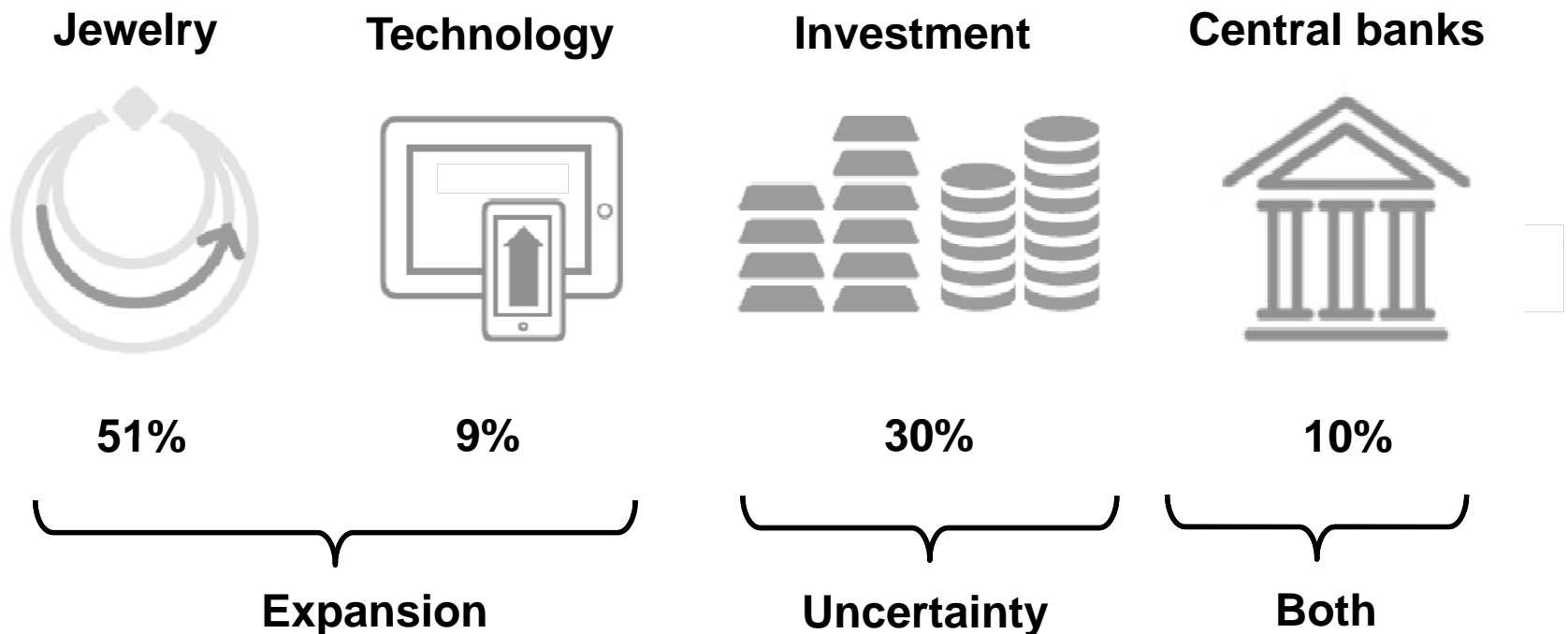
Emerging market  
demand  $\approx$  70%\*

\*Based on **10-year average demand** estimates ending in 2018. Includes jewelry, technology, bars, coins, and ETF demand. Excludes over-the-counter transactions and central bank purchases.

Source: Refinitiv GFMS, World Gold Council

# Dual nature of strategic demand

Average annual demand  $\approx$  4,350 tonnes\* (approx. US\$177bn)

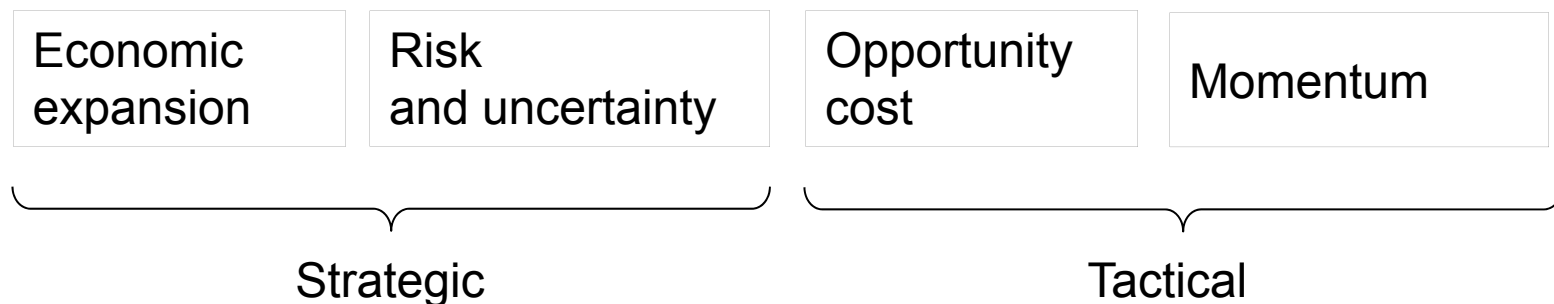


\*Based on 10-year average annual demand estimates ending in 2018. Includes jewelry, technology, bars, coins, and ETF demand. It excludes over-the-counter demand. Figures may not add to 100% due to rounding. US dollar value computed using the LBMA Gold Price as of December 2018.

Source: Metals Focus, Refinitiv GFMS, World Gold Council

# Drivers of gold

- **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 such as bonds (through interest rates), currencies and other assets, influence investor attitudes towards gold
- **Momentum:** capital flows, positioning and price trends can ignite or dampen gold's performance.



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