Opinion **Markets Insight**

Gold bubble should prompt central banks to sell the metal

The world is a thoughtless prisoner of history when it treats bullion as a desirable store of value

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Gold is extracted underground at material cost, turned into bars and then put back underground at additional cost © Andrey Rudakov/Bloomberg

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In 2009, I wrote that gold was in the midst of a 6,000-year-old bubble. Since then, it has continued to defy my scepticism over the intrinsic real value of the metal which I believe is basically de minimis. Back when I made my bubble remark, gold traded at $1,109 an ounce. Now, after more than a 50 per cent increase since the start of the year, it is trading above $4,000 an ounce.

Gold is sometimes compared with bitcoin as an investment for those worried about the debasement of fiat money, and I likened the inherent properties of the metal to the crypto asset in 2014.

There are some similarities, not least volatility. Bitcoin has risen even more spectacularly than gold, from around 20 cents in November 2009 to $122,000 — just below its all-time high. Bitcoin also has experienced even more spectacular price drops than gold. Its price declined by 74 per cent between October 2021 and December 2022. The largest proportional fall in the price of gold this century was nearly 44 per cent, between 2011 and 2015.

As a free-floating, digital cryptocurrency, bitcoin is worth whatever the market thinks it is worth, which could be $2mn or nothing. While the total stock of bitcoin outstanding is capped at 21mn units, a skilled collection of cryptographers could create any number of identical replicas of capped bitcoin.

But bitcoin might be valued as a means of payment, which is not something gold is particularly useful for. While the stock of physical gold also is capped, why anyone would prefer the metal as a means of payment to digital currencies, especially ones from central banks or fully backed stablecoins, is a mystery to me.

The inherent value of gold remains insignificant. Yes, there is consumption demand for gold as jewellery. Of the total 216,265 tonnes of above-ground stock of gold at the end of 2024, jewellery accounted for 97,149 tonnes (45 per cent). I believe that much of this "consumer demand" — indeed most of it — is in fact investment demand. Only gold coins and bars (including exchange traded funds) are counted as investment demand. At the end of 2024, this accounted for 22 per cent of the total stock. Central bank holdings were 17 per cent. Gold's use in technology accounts for part of the 15 per cent of the global stock, classified as "other".

It is possible that an increase in gold use in electronics driven by the spectacular advance of artificial intelligence and continued dental demand set a positive fundamental price of the metal. I doubt this is anywhere near the cost of extraction, storage and insurance. Costs of gold extraction vary widely, but the World Gold Council estimated the all-in cost at around $1,500 per tonne in the first quarter of this year.

The flow supply of new gold in 2024 was 4,975 tonnes — a costly waste of resources. I recognised this when, as a member of the Monetary Policy Committee of the Bank of England, I was shown the physical gold reserves stored in the bank's basement.

Gold, extracted underground at material cost, was turned into gold bars and then put back underground at additional cost. Globally, gold reserves (ore deposits that can be economically extracted) are estimated at 54,770 tonnes and gold resources (ore deposits where the profitable extraction is more doubtful) at 132,110 tonnes. The only gold production strategy that makes socio-economic sense is to leave it all in the ground.

It is true that trade in derivatives sharply reduces the cost of using the existing stock of gold as a means of payment and store of value. It is easy to envisage a world in which digital gold derivatives can be held and traded on blockchains and other efficient decentralised finance mechanisms. The underlying physical gold, however, will always be costly to extract and store safely.

The world is a thoughtless prisoner of history when it treats gold as a store of value, particularly central banks, which have seriously increased their holdings of gold since 2022 — by more than 1,000 tonnes each year, according to the WGC. At the end of 2024, gold holdings accounted for 20 per cent of central bank reserves, more than euro reserves (around 16 per cent). Gold's price surge since would have pushed its relative share higher. No central bank should invest in a single physical commodity, especially one with negligible intrinsic value and massive risk. There will be no resurrection of the gold standard.

Individuals and investment firms considering investing in gold should do so only if you can afford to lose most or all of this investment. Central banks should sell as much as possible to any such private agents that meet this criterion.

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