The London Gold Fixing

The standard behind the fluctuating gold price

The Gold Fixing Room, N. M. Rothschild & Sons, New Court, St. Swithin's Lane. Reproduced with the permission of The Rothschild Archive.

The London Gold Fixing, formally adopted on 12 September, 1919, is the standard by which the market price for gold is set, twice daily during trading, at 11:30 and 15:00 (Greenwich Mean Time / British Standard Time). It began with five bullion brokers: Mocatta & Goldsmid, Pixley & Abell, Sharps & Wilkins, Samuel Montagu & Co. and N. M. Rothschild & Sons. The original five participating banks have since vacated or been acquired, or have merged with other entities; and its numbers have since doubled to over ten banks. The process of fixing the gold price works by establishing the price at which the gross amount of gold placed on buy orders matches the gross amount of gold on sell orders across all of the participating banks. If the net effect across all the participating banks is in balance, the price is fixed—an action carried out by the chair.

Under the old system, the fix took place on the premises of N. M. Rothschild & Sons, whose representative acted as Chairman. Each participating bank had a representative of its own, all sitting together, equipped with telephones and Union Jacks. Flags were raised to signal a desire to pause the dealing process. The term 'flag up' is believed to be derived from this peculiarity. There is some debate as regards the earliest point in time when the gold fix was first introduced. Was it conceived in 1919, or did this date represent a resurrection and reconfiguration of a formalized pricing ritual? An excerpt in the Wall Street Journal of 1907 entitled “The World’s Gold Market” hints at the fix being a far more formal affair, prior to the Great War, than originally first thought:

"…if a stranger was to stop an average Londoner, to ask him the way to the 'gold market', he would be answered with a stare of amazement. Even among the city numbers, there are few who have actually seen the mechanism they admire so much. It is probably a mystery to them as to the ordinary public how gold is handled in London…At a place which, for obvious reasons cannot be divulged, the bullion brokers meet punctually at a quarter to two o'clock. Some, or possibly all, of them have certain amounts of the precious metal to dispose of. Others may have buying orders, and there is nothing to prevent a broker acting for both sellers and buyers…By way of concrete example we may take their meeting of one Monday last month. It was an unusually interesting day, and very significant of the existing situation. The demand for gold was keener than ever, and there were a good many small buyers in the market. The action of the Bank of England was uncertain, and still more so was that of the New York banks. Though the price was fixed at 77s. 9⅜d. [77 shillings and 9⅜ farthings], it was a question if the Americans might not go a fraction better. The Bank of England intimated through its broker that it would like to have all the gold available and would give 77s 9⅜d. for it. There is at present a tacit understanding that the bank is to have preference when it is willing to pay the best bid by any other buyer. In one corner of the city, there is thus a faint survival of nobles oblige. The bank exercised its call on Monday's gold. From the board room, the bullion brokers rushed to their offices. There, telephones and telegraphs were set in motion to report results to clients in various parts of the world. Cable messengers reached New York almost as soon as an office in Throgmorton Street could be called up. Answering rings were soon heard, most of them inquiries from buyers who had been impatiently waiting the result of the official board."
~ Wall Street Journal, 20 April, 1907

The stage was set for a new order of economic notoriety for the City of London. It had been neither coincidental, nor without foundation that the aforementioned trading hub was tasked with fixing prices on precious metals. By the conclusion of the First World War, the London Gold Fixing sprung up from the Bank of England's desire to restore the international importance of sterling, and reenergize the City of London's markets. The London gold market was one such market. Thus, the Bank of England determined that South Africa's gold must be marketed in London. To accomplish this goal, it had negotiated agreements with the South African mining companies to ship their gold to London, where the precious metal would be sold through intermediaries in the market via the bullion brokers. By the first fixing, on the 12th of September, 1919, the City of London was re-established as an international financial centre and clearing house.

The gold price was quoted in sterling from 1919 until 1968, before it was superseded by the U.S. dollar. So was the afternoon fix also introduced, to accommodate overseas markets in New York. N. M. Rothschild & Sons hosted and chaired the gold fix since the very onset. In April 2004, it gave notice of its pending withdrawal; a process made complete in June 2004, when Barclays entered the fray in its place. The chairmanship of the gold fix, formerly held exclusively by N. M. Rothschild & Sons, was reformed to rotate annually. These past developments have come with their share of drawbacks. With the last of the original five founding banks now gone, coupled with the increase to more than double the size of the participants, the discipline of the standard took on a different aura, and the means of scrutiny in place to deter banks from manipulating, rigging and price fixing were rigorously tested. The fixing room in St. Swithin's Lane was replaced with conference calls between the participating bullion brokers.

On 23 May, 2014, the Financial Conduct Authority, a financial regulatory body based in the United Kingdom, slapped Barclays Plc with a £26 million fine for systems and controls failures, and for conflict of interest in relation to the gold fixing over the nine years to 2013, and for manipulation of the gold price on 28 June, 2012, whose trader Daniel Plunkett was fined £95,600 and banned for life from the industry. Similarly, on 25 July, 2014, a lawsuit was filed in a New York district court alleging that Deutsche Bank, HSBC, and Bank of Nova Scotia had manipulated the silver price.

When we closely observe a chart depicting a forty year trend of the gold price, we can draw the following conclusions: (1) the gold price has surged in value in recessionary times, namely during the early 1980s recession and the 2008 financial meltdown; (2) the gold price has remained relatively stable in between these global recessions, with prices fluctuating in the region of $400 per troy ounce; (3) bullion brokers and traders heavily speculated on precious metal commodities at the height of the 2008 recession, opting to hoard gold, in effect by divesting capital from stocks and shares and shifting resources over to gold which otherwise could have been spent elsewhere; (4) the gold price has risen to well above its natural levels in the periods spanning 2008-2012, to a point where in 2008 and mid-2011 to 2012, gold was worth in excess of platinum; (5) the global recession relented by mid-2014 and the gold price contracted to reflect the shift in capital resources from gold over to stocks and shares; (6) the unfolding pattern suggests a correlation between economic recessions and inflationary gold value.

On 18 June, 2014, the World Gold Council, a marketing body for gold producers and consumers, called to convene a debate in July on the issue of phasing out the standard that had been in place since 1919, in order to reform it with an electronic replacement. This novel approach had been tried and tested on 15 August, 2014 when the silver fix entered the digital age, during which an algorithm system administered by Thomson Reuters and CME (Chicago Mercantile Exchange) was used, for the first time ever on any precious metal, to set the benchmark price for silver. The platinum and palladium replacements followed suit on 1 December, 2014. The gold fix would be next in line.

On 20 March, 2015, the London Gold Fixing underwent similar reforms as the silver, platinum and palladium fixings when ICE Benchmark Administration took on the task of running the digitized system, which replaced the 95-year old fix of 1919. The gold price was, under the previous system, set by bullion brokers through conference calls. Under the new system, the gold price is settled via an electronic and tradable auction. The digitized systems for the precious metals (gold, silver, platinum, palladium) were initiated by the LBMA (London Bullion Market Association), an international trade & commerce association for precious metals based in the City of London.

The notion that gold increases in value when compared with anything else of tangible value is a flawed concept. Gold appears to increase in value as a result of deflationary fiat currencies. This is because fiat money is backed by the confidence one has in its purchasing power, and not by anything of tangible value, like e.g. gold or silver. The moment that people lose confidence in its purchasing power, as was the case with the greenback in the American Civil War, money seizes to have currency and depreciates in value, until it is phased out by market forces. Commodities like gold, however, are more robust because of their intrinsic value. G. Edward Griffin illustrates this point:

"…if we had lived in ancient Rome and had a one ounce gold coin, we would have been able to buy a fine toga, a hand-crafted belt and a pair of sandals. That was the price. So, today, what can we buy with a one ounce gold coin? We can walk in to any men's store and buy a really fine suit, a hand-crafted belt and a pair of shoes. The real price of these items hasn't changed in thousands of years when expressed in terms of real money!"

~ G. Edward Griffin