ISSUE BRIEF

World Platinum Investment Council

Platinum's inclusion in Central Bank reserves

Background

The role of Central Bank reserves is to provide a reserve for the creation of stability in currency and balance of payments management and to provide a cushion during times of stress. Historically these reserves protected against stresses resulting from liquidity, solvency, inflation and external economic shocks.

In general the IMF requires that reserve assets always refer to assets that actually exist. Credit lines, guarantees and central bank swap arrangements are not recognised as actual assets and, therefore, are not reserve assets although in certain circumstances forward contracts and options may be eligible. Gold and platinum remove any doubt in terms of credit or counterparty risk.

Central Banks favour assets that are liquid, have little or no credit risk and which diversify their holdings and have low correlations with other asset classes and financial markets.

Gold's inclusion in central bank reserves is widespread and long-standing. If a small portion of platinum is added to, or supplemented for, gold the risk adjusted returns improve.

Platinum qualifies as a reserve asset and improves central bank portfolios:

- Platinum satisfies the criteria for its inclusion as a central bank reserve asset, WPIC believes. Platinum provides typical central bank assets with similar diversifying benefits to that of gold.
- The inclusion of platinum in a typical central bank portfolio improves risk adjusted returns and enhances recovery from stress events.
- OECD guidelines and the IMF Balance of Payments Manual provide adequate flexibility for the immediate inclusion of platinum, in WPIC's view.
- Platinum is adequately liquid to qualify as a reserve asset. Liquidity in platinum is the result of trade in the London OTC spot market, the NYMEX and TOCOM futures exchanges and in global ETF markets. Daily trade of 200 000 oz is not unusual. While the liquidity of gold is greater than that of platinum if the portion of platinum held by a central bank was less than 20% of its gold holdings the platinum liquidity within the central bank portfolio would be similar to that of gold.

The reasons platinum improves performance of central bank assets include:

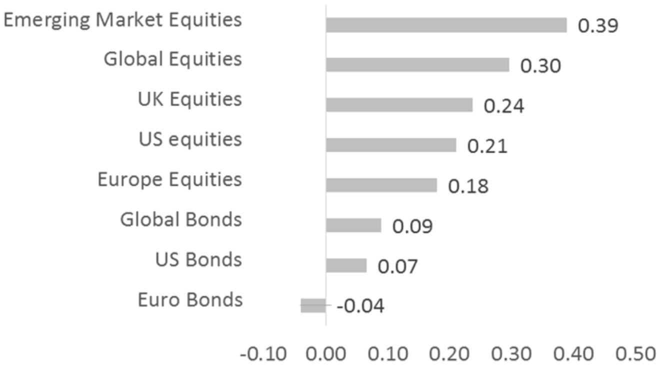
- Platinum has a low correlation with equities and bonds (see Figure 1).
- Platinum has a low correlation with equities during times of crisis (see Figure 2).
- Platinum improves risk adjusted returns across a number of portfolios and across a number of currencies (see Figure 3).
- Platinum returns from 1999 have outperformed reserve assets other than gold despite recent price weakness. Platinum has risen by 8% per annum on average since 1999 (see Figure 4).

South Africa has additional strategic benefits from including platinum as a reserve asset:

- Platinum is a natural hedge against a South African country crisis. The high proportion of global platinum supply from South Africa would be jeopardised by a country crisis and global demand for the balance of supply would increase the value and liquidity of platinum reserves.
- The inclusion of platinum in the reserves of the South African central bank (the South African Reserve Bank, 'SARB') is likely to lead to other central banks including platinum in their reserves and over time formal IMF support could increase this even further.
- Increased central bank holdings of platinum as a reserve asset would increase global liquidity in platinum.

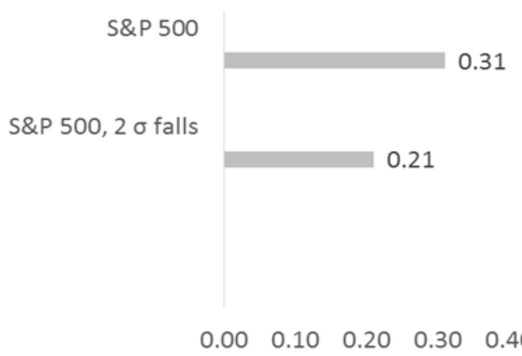
Figures:

Figure 1: Platinum has a low correlation with equities and bonds



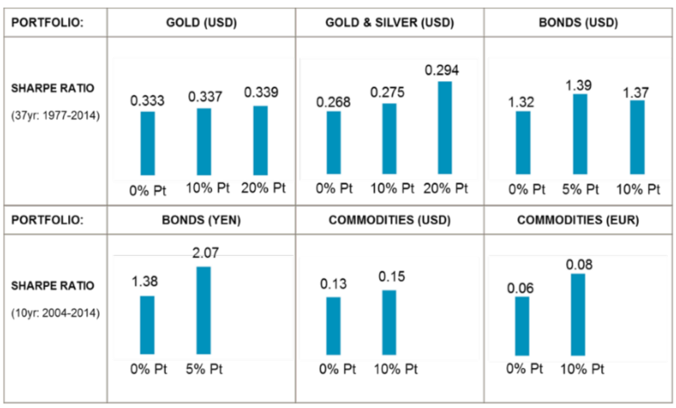
Source: Bloomberg, WPIC analysis. Note: Monthly return correlations back to 1998

Figure 2: Platinum has a low correlation with equities during times of crisis



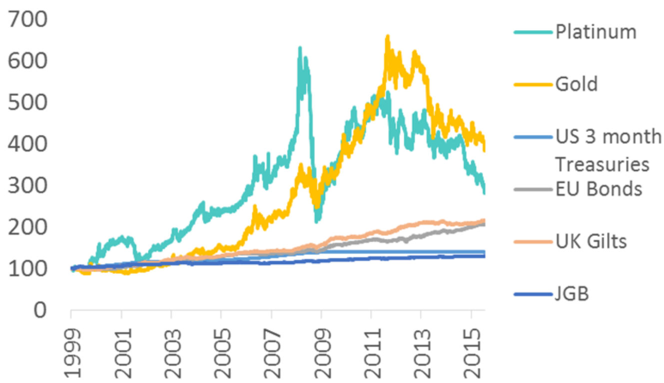
Source: Bloomberg, WPIC analysis. Note: Monthly return correlations back to 1998

Figure 3: Platinum improves risk adjusted returns across a number of portfolios and across a number of currencies



Source: WPIC commissioned research by Exocet Advisory. Note: Selected results from analysis across several asset classes and currencies.

Figure 4: Despite recent price weakness platinum has outperformed most central bank reserve assets, excluding gold. Platinum has risen by 8% per annum on average since 1999



Source: Bloomberg