THE DECEPTIVE LURE OF RECYCLED-ONLY GOLD

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We consider gold, with its unique behavioural traits, to be an important building block to consider for any portfolio. The metal's price can behave defensively which is typically very beneficial in times of economic shocks and it also tends to respond well to inflation which can be beneficial in times of economic growth. Like any core component of a portfolio, we must consider its responsible sourcing and environmental social and governance (ESG) factors.

ESG is complex and multidimensional

For commodities like gold, it is often unclear what ESG factors really mean as the concept of extracting, refining and eventually storing the commodity may have severe impact on the environment and local communities. Improving on environmental standards may come at the cost of social standards (and vice-a-versa). Each investor/consumer is likely to have a slightly different vision on ESG. In a prior blog post we have discussed the concept of responsible sourcing and the standards developed by the London Bullion Metals Association (LBMA)[1].

Focusing on recycled-only gold is a red-herring

Some market participants promote recycled gold as the holy grail of ESG friendly gold. Indeed, gold is infinitely recyclable and given that most gold above ground is easily mobilised it has the highest recycling rates of any metal. Since its discovery, only 2% of all the gold mined is unaccounted for[2], either having been dumped or lost track of. Gold is simply too expensive to be thrown away, which encourages high rates of recycling.

According to the World Gold Council, 205,238 tonnes of gold have been mined through history to 2021, with about two-thirds since 1950[3]. Since gold is infinitely recyclable, this means that almost all of this metal is still around in one form or another. This means that the above-the-ground stocks represent nearly 60 years of current annual mining production. Knowing that the majority of this gold (85%)[4] is very easily recyclable because it is in the hands of individuals and central banks and in a high-grade form (privately owned investment gold: 45,456 tonnes, jewellery: 94,494 tonnes, central bank: 34,592 tonnes) it means that newly annual mined gold (3,560.7 tonnes in 2021) represents a little more than 2% of this easily acquirable or 'near-market' recyclable gold stocks.

Not only is almost all gold already being recycled, but the vast majority of the gold processed by LBMA Good Delivery refiners is recycled[5]. All gold in the London over-thecounter bullion market (and thus the bars backing gold ETPs) are LBMA Good Delivery. Hence the average LBMA bar should already have a high recycled content.

The numbers painted above indicate that it is almost impossible to significantly increase the volume of recycled gold. Therefore, by choosing a recycled-only strategy for improving ESG in a gold bar is likely to have zero impact on the market and the environment. It serves as a cheap way of window-dressing, for those who want to tick boxes. At a micro level, the bar may have a low green-house gas (GHG) footprint, if you only look at mid to downstream emissions, but the full life-cycle of the bar (i.e. including mining the original material) would have a greater GHG emissions. For those that want to change business practices in the gold industry, effort could be directed elsewhere.

Ignoring new gold will likely diminish overall ESG standards

Not all demand for gold can be met through recycling. Without consumer and investor pressure and appropriate oversight of the miners and refiners, newly produced gold is unlikely to improve in ESG metrics. We believe the only way to improve environmental and ethical standards in the gold value chain is to attack any issues at the source and to ensure that any new gold entering the system meets the highest possible ESG standards (and that any remaining adverse impacts are offset). We believe investors can exert their influence on newly mined gold. If investors simply buy recycled-only and turn a blind eye to the rest of the market, their influence is lost.

Chain of custody and provenance risks could rise with excessive recycling

Its not just that recycled-only gold has no meaningfully positive impact on the environment, it may in fact encourage excessive ‘churn’ in gold. That raises the risk of gold from questionable sources entering the recycling pool. While the LMBA and Responsible Jewellery Council (RJC) encourage strong processes to exclude gold from questionable sources, not all gold passes through their oversight[6]. The chain of custody may be lost after several recycles for example and start to creep into the ‘legitimate’ pool.

Metals Focus data shows that the main source of recycled material is old scrap (28% of total gold supply over the 2010-2021 period)[7]. Old scrap is defined as the entirety of gold that has gone into jewellery, electronics, dentistry, decorative applications, miscellaneous industrial and medical uses. Bars (whether minted or cast) by their definition can never become part of scrap as by definition they have remained in bullion form and have never become a fabricated product. Process scrap - the material that forms part of the circular flows between a refiner and a fabricator[8] – don’t normally form part of the recycling statistics. The lines between process and old scrap can be blurred. According to Alliance for Responsible Mines, **the main standards adopted by the jewellery industry include fabrication scraps as eligible material into recycled gold (although it’s unclear if that is the standard applied by RJC members). The Alliance for Responsible Mines claim that some fabrications, particularly in the luxury segment, can generate more than 50% scrap. This increases the risk that recently mined gold can be introduced as recycled products just a few weeks after its extraction**[9].

Conclusions

In summary we believe the best way to consider ESG factors for investment products backed by physical precious metals is to tackle the issue at the source and to ensure the product optimises and mitigates any adverse impacts from initial sourcing/mining throughout the entire value chain. By incentivising the production chain to minimise and offset any adverse impacts and to optimise the GHG footprint, investors can have an actual impact on the gold in circulation.

Sources

[1] See Responsible gold sourcing: the gold standard in bullion sourcing

[2] According to Alliance for Responsible Mining

[3] https://www.gold.org/goldhub/data/how-much-gold

[4] Assuming jewellery, bars (including those in ETPs), coins, and central bank reserves are all easy to move.

[5] 55%, according to article written by Sakhila M. Mirza, Executive Board Director and General Counsel, London Bullion Market Association (LBMA) in Singapore Bullion Market Association.

[6] We map out the gold supply chain and oversight here: https://www.wisdomtree.eu/en-gb/strategies/responsible-gold/gold-infographic

[7] Spotlight On Gold Recycling, Prepared by Metals Focus for LBMA, April 2022. Their definition of scrap excludes bullion (unlike LMBA)

[8] For example, gold sheets to be turned into coins, where there is waste around the circle stamped out. The extra gold is never fabricated, but goes to back to refiner.

[9] https://www.responsiblemines.org/en/2019/10/is-recycled-gold-an-ethical-choice/

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