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Research Note 54

## **Brown's Gold Sales: The £5 billion mistake**

Between January 1999 and July 2002, the Treasury sold 395 tonnes of gold from the United Kingdom's reserve holdings. The sale – authorised by Gordon Brown, then Chancellor of Exchequer – raised around \$3.49 billion (£2.16 billion), which was then reinvested in interest-bearing foreign currency assets. There has been widespread criticism of the decision, as the gold price has since risen rapidly for a sustained period.

Criticism has been particularly acute as the sale appears to have been the result of a Treasury decision taken with little consultation. It has been established by the *Sunday Times* that:<sup>1</sup>

- The Bank of England was never asked for its advice on whether Britain should sell the gold.
- At a secret meeting with senior gold traders, Bank of England officials were warned that the proposed auctions would achieve the worst price for taxpayers. The officials agreed but said they were powerless to influence the Treasury.

Many attempts have been made to assess the gold sale, this research note provides the most comprehensive and up to date estimate of the extent that the decision to sell gold and buy interest-bearing foreign currency assets has meant that the taxpayer losing out on a substantial increase in the gold price, and billions of pounds.

### **Key findings**

- The **loss from selling gold** and buying interest-bearing foreign currency assets is around **£4.79 billion, or around £192 per household**.
- Since the gold sale, the gold price has risen from around \$275 per ounce to nearly \$1,120 per ounce. At that price, the **gold** that was sold **would now be worth around £8.71 billion**. That means the foregone nominal increase in the value of the gold sold is around £6.56 billion.

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<sup>1</sup> Winnett, R. & Watt, H. 'Brown lost £2bn selling UK's gold', *Sunday Times*, 15 April 2007



- That is not entirely a loss though, as the money was reinvested in **interest-bearing foreign currency assets**, which have also provided a return. It is reasonable to expect that those investments are now worth around **£3.93 billion**.
- The collapse of Barings Bank, at the hands of “rogue trader” **Nick Leeson**, came after **£827 million in losses**. The **loss on the gold sale** is more than **five and a half times as large**.

Matthew Sinclair, Research Director at the TaxPayers' Alliance, said:

*“When he was at the Treasury, Gordon Brown sold billions of pounds worth of our gold reserves at the very bottom of the market. Taxpayers have lost out on billions that are sorely needed as they face paying the price for his other mistake of pursuing a profligate spending policy, mistaking a temporary boom for a permanent improvement in our economic fortunes. It is clear that the Prime Minister’s management of the nation’s finances was disastrous and this Christmas taxpayers might just be grateful he didn’t get his hands on our frankincense and myrrh.”*

To discuss the research and arrange broadcast interviews, please contact:

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## Sources and Methodology

The average price when the gold reserves were sold and the amount sold have been provided by the Treasury<sup>2</sup> and the amounts in dollars can be converted to pounds at an exchange rate of 0.6182, the exchange rate at 1 January 2000.<sup>3</sup> As mentioned earlier, the sales took place over a protracted period but using the exchange rate at the beginning of 2000 gives a reasonable estimate.

Price	\$274.92
Tonnes sold	395.00
Ounces sold	32,150.75
Value	\$3,491,358,882
<b>Value</b>	<b>£2,158,358,061</b>

At 7.14am 15 December 2009 the gold price was \$1,115.10.<sup>4</sup> That is a very rapid rise since the sale, which is marked with a circle on this 30-year graph of the gold price and known as the “Brown bottom” in the investment community:



<sup>2</sup> HM Treasury 'Review of the sale of part of the UK gold reserves', October 2002, paragraphs 1.1 and 6.28

<sup>3</sup> Historical exchange rates are available from: <http://www.oanda.com/currency/historical-rates>

<sup>4</sup> Bloomberg market data

As a result, Britain has foregone a substantial nominal increase in the value of the gold sold:

Price	\$1,115.10
Tonnes	395.00
Ounces	32,150.75
Value	\$14,161,262,512
<b>Value</b>	<b>£8,713,424,824</b>
<b>Increase in gold value since sale</b>	<b>£6,555,066,763</b>

That does not mean that the gold sale led to a £6.5 billion loss, though. The money was reinvested elsewhere, and those investments will have yielded a return. To assess the amount gained or lost from the investment decision we need to compare the returns on the two investments.

The Treasury reports that:<sup>5</sup>

*“The portfolio that has arisen following the sales can be modelled by assuming that the proceeds of each auction are reinvested in interest-bearing foreign currency assets (e.g. US T-bills and Treasuries, euro government bills, euro government bonds and Japanese financing bills) in the proportions 40% dollars, 40% euros and 20% yen. This reinvestment of auction proceeds took place shortly after each auction in line with the wider investment policy for the net reserves.”*

The reinvestment of the money raised in the gold sale in that package of interest-bearing foreign currency assets would have yielded the following return:<sup>6</sup>

Dollars	
Invested	\$1,396,543,553
Growth rate: 2yr US Treasury bonds	3.25%
With 10 years growth	\$1,922,892,863
Value	\$1,922,892,863
Euros	
Invested	€1,386,767,748
Growth rate: 2yr German Government bonds	3.22%
With 10 years growth	€1,903,891,873
Value	\$2,788,359,510

<sup>5</sup> HM Treasury ‘Review of the sale of part of the UK gold reserves’, October 2002, paragraph 6.10

<sup>6</sup> Growth rates are averages from Bloomberg market data, initial exchange rates are for 1 January 2000 and final exchange rates from 15 December 2009

Yen	
Invested	¥142,880,370,904
Growth rate: 2yr Japanese Government bonds	0.36%
With 10 years growth	¥148,078,684,361
Value	\$1,669,532,502
Total	
Total value of investments	\$6,380,784,875
<b>Total value of investments</b>	<b>£3,926,096,933</b>

Comparing the return on the actual investment in interest-bearing foreign currency assets with the value of the gold now yields the following result:

Total value of Treasury investments	\$6,380,784,875
Potential value of gold sold	\$14,161,262,512
Amount lost	\$7,780,477,637
<b>Amount lost</b>	<b>£4,787,327,890</b>