Metals Strategy: Review of the LBMA OTC volumes & positioning data and size of the Gold market

Will the data become the equivalent of the COT data for the forward market?

The LBMA announced in October that it would begin publishing weekly data (5 day aggregate volumes) showing total OTC trading activity of its LBMA members. We only have 2 data points after the first release last week, and the data will become more insightful once theres a trend. However, its somewhat worthwhile to do a deeper analysis of the size of the (historically opaque) London Gold & Silver market, and to outline some thoughts on positioning and relative liquidity (not any directional price outcomes) in light of this new initiative to become more transparent.

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The analysis below slices the data several ways. Summary:

- **If daily average volumes is a proxy for the size and liquidity of the OTC Gold market, then at $32bn, Gold is 1.3x larger than LME Copper, 2.4x larger than the Chinese paper market, 36x larger than GLD ETF, and 6x larger than the worlds largest equity by market cap, Apple.**
- **However, the OTC Gold market is still smaller than the CME paper market (which is 1.3x larger), the US Treasury Bills market (3.4x larger), and the WTI Market (1.9x larger), as 'expected'**
- **Gold OTC positioning (excluding leases & options), stands at 61mn oz, which is 47% larger than aggregate open futures positioning on its rival/sister paper hub (CME).**
- **Overall, the expectation that OTC London liquidity would be much larger than paper NY is being dialed back with these volumes figures, but note that overall London Gold positioning (the underpinning foundation of all financialized gold trading) is much larger.**
- **A Gold liquidity gauge (or HFT participation rate?) can be measured by daily volumes as a % of the "pie" (total positioning or metal vaulted):**
- **OTC volumes are 11% of the its vaulted gold; CME volumes represent 82% (of total OI positioning) and ETFS (GLD) represent 3% of GLD Holdings.**
- **this outcomes drastically highlights the larger participation of systematic, HFT or intraday traders on CME and how 'financialized' exchanges have become - its pretty clear that the daily "churn" (ie: high daily volumes relative to flat or low positioning, or metal available) is highest for the NY exchanges where most of this arguably "uncommitted" activity takes place.**
- **The size of the Silver market (as measured by average daily OTC volumes) is 338mn oz (~$4.9bn). The Comex Silver market is also relatively larger than the OTC market with average futures 1.4x larger.**
- **Potential risks and outcomes due to the release of the data:**
    - **Will the data become the COT data for the gold forward market? Theres a risk that the forward market becomes "financialized" and the barrier to entry into the London forward market is lowered, as there will be a key input - the availability of activity & positioning data - for any CTA, HFT or algorithmic systems to chew on and internalize.**
    - **By affirming the size of the historically unknown daily transactions, would this make Gold more susceptible to the actual availability of metal (i.e.: it trades more as commodity where forward rates are sensitive to S&Ds) or will it remain a rates/financing product contingent on the availability and liquidity of the dollar and currencies**
    - **Overtime if the OTC data conforms to and proves liquidity expectations, that bodes well for lobbyists aiming to reduce Golds handicap (at 50%) in relation to Basel III liquidity requirements (NSFR). Gold liquidity – and the belief that its a High Quality Liquid Asset (HQLA) – is a large and important reason why structural players (asset managers, pension funds, central banks, etc) allocate to Gold**
    - **LBMA Volumes and OTC positioning could potentially become especially interesting around seasonal inflection points where lending is a larger feature**
- **An equivalent PGM trading & positioning report (perhaps in January 2019 when the data release changes to T+1?) would be more insightful and interesting not only because they are relatively smaller and more fundamentally driven markets, but also because of the lack of (or perceived lack?) of Palladium liquidity and volumes in Zurich and London.**
- **There are questions around some of the methodology in order to understand the data better and understand if and where there could be any double counting.**

Background:

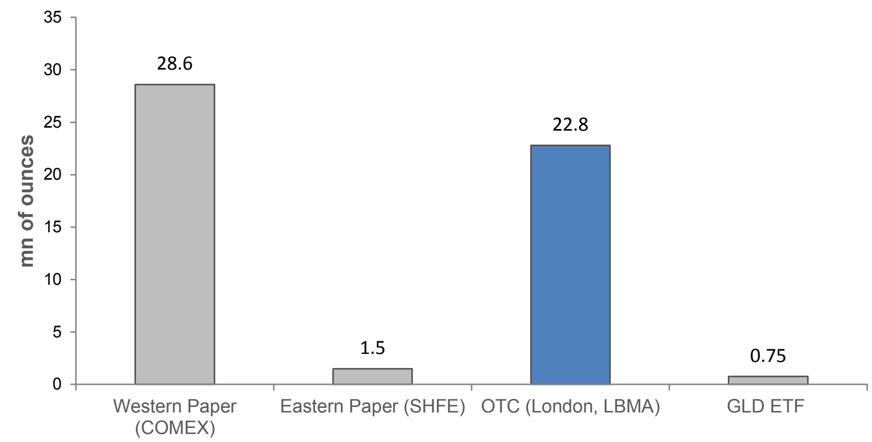
- **The data: content, definition and release schedule: almost all Gold & Silver OTC activity, not everything**
- 2 reports of gold and silver data are published on a weekly basis, each Tuesday at 9am GMTG and represent:
- Daily Trading Volumes by transaction type & duration: covers London & Zurich volumes of LBMA members as an average in ounces taken over the previous five-day (Friday-Friday) reporting week period. Its analogous to the available liquidity and activity of the OTC Gold market, and also breaks down the data by transaction type (spot, forward, option & lease/deposit) and by time period (spot, 1week, 3mo, 1yr+ etc)
- Open Trades by transaction type & duration: this is analogous to positioning (or Open Interest), and is a running total of all members open trades that don't expire on the stated date, reported both by times buckets & transaction type
- These 2 reports show the size and liquidity availability (in ounces) of the OTC market, represented by the LBMA Full members (13 market makers - largely banks – and 29 reporting entities), but it doesn't include non-LBMA member to non-LBMA member transactions.
- The intention in Q1 2019 is to move to daily reporting on a T+1 basis (which will then become a licence/paid subscription service…) and to provide PGM data. Downloadable here http://www.lbma.org.uk/lbma-i

- **Why now?**
- Greater transparency is an overarching theme for almost all markets after 2008. Until now, the size of the London gold market will no longer be a guestimate but a reliable measurement which can be tracked over time for better insight no just on the size of the market, but the shift in forward, option and leasing positioning across the curve
- It follows other key "transparency" drives within the precious metals markets such as improved and timely Central Bank activity data from the IMF and WGC, LME eventually producing a COT report showing investor flows and positioning, data on London vault holdings, and timely releases of key import/ export metals flows into key trading regions/hubs.

1. Overall size of the London OTC Gold & Silver markets (Total Volumes Report):

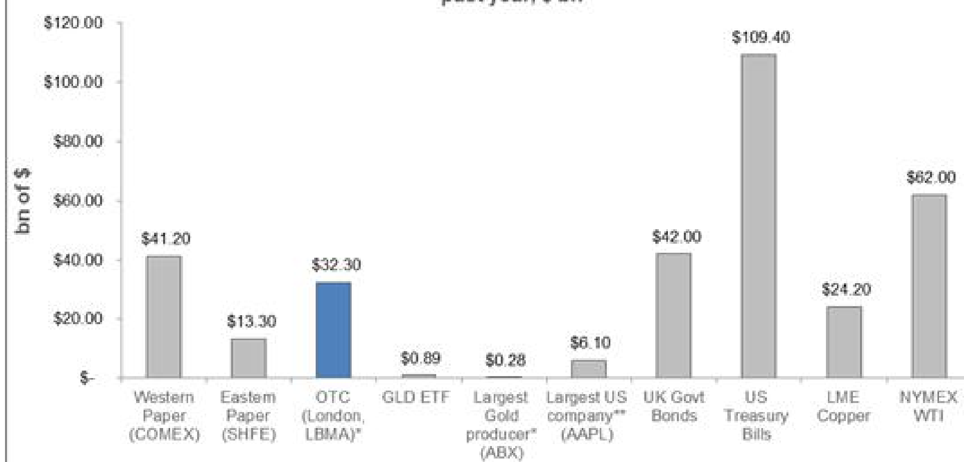
- Over the last 2 weeks the daily average volumes traded in the OTC Gold market was 26.5m oz (~$32.3bn)
- Currently, 63% of the Gold activity were spot transactions, 29% forwards (down from previous reporting week of 31%), 2% options and 5% Loans/Leases (up from 4% the previous week).
- The average daily OTC volumes in Silver (over the last 2 weeks) were 338mn oz (~$4.9bn)
- That's currently broken down to 62% spot (up a decent amount from the 59% the previous reporting week), 31% forwards, 4% options (up from 2% due to tripling of 3month option activity) and 2% Loans/ Leases.
- The Comex Silver market is still relatively larger than OTC with average futures 1.4x larger
- If daily average volumes is a proxy for the size and liquidity of the market, then the OTC Gold market at $32bn is:
- Larger than the Chinese paper market (OTC gold is 2.4x larger), the GLD ETF (36x), LME Copper (1.3x), ABX (120x) and Apple (6x), which seems somewhat surprising.
- Smaller than the CME paper market (CME is 1.3x larger than OTC Gold), the US Treasury Bills market (UST is 3.4x larger), and the NYMEX Oil market (almost 2x larger) which is as 'expected'
- Overall, the expectation that OTC/London liquidity would be much larger than NY/futures is being dialed back with these figures, but note that overall London Gold positioning (next paragraph) is much larger.

OTC Gold activity vs. other major hubs & platforms - average volumes between paper, OTC and equity proxies, during the reporting week (Nov 19 - 23)



Source: Scotiabank Commodities Strategy, LBMA-i, Bloomberg

OTC Gold activity vs. other related products - average daily volumes traded the past year, $ bn



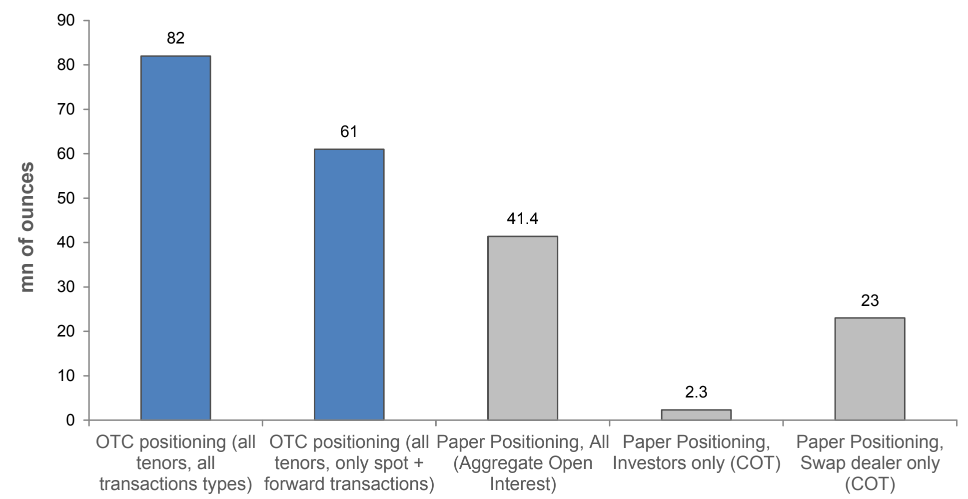
*ABX, after RandGold acquisition, will become the world largest Gold producer . Volumes aggregated across US & Canadian Exchanges
** Largest by Market Cap

Source: Scotiabank Commodities Strategy, LBMA-i, Bloomberg, AFME, SIFMA

2. Overall availability, positioning and breakdown of the the London OTC Gold & Silver markets, by transaction type: (Open Volume Report):

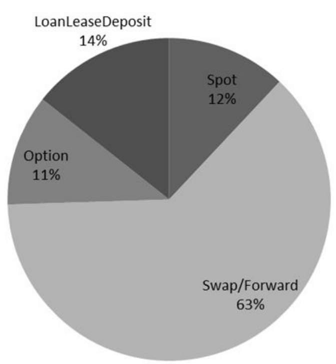
- Currently theres 82 mn oz in of OTC open positioning spanning spot out to 1+ year tenors with the bulk of positioning in Swap/ forwards (63%), as expected.
- That is double the size of the Aggregate Comex futures positioning (measured by Aggregate Open Interest). However the OTC positioning (excluding leases & options), stands at 61mn oz, which is still 47% larger than aggregate open futures position, and much larger than the swap dealer positioning (of 23mn oz), indicating that there could be some double counting in the report.
- In Silver, theres 1.1bn across all tenors and all transaction types, with relatively larger (vs Gold) positioning in swaps/forwards, of 68%. Theres almost 900mn in just spot & forward (excluding leases & options) positioning, which, unlike Gold, is actually less than the aggregate futures open interest of 940mn oz.
- Overall, the open positions of the London Gold market is relatively larger than the open positioning in its rival/sister paper hub (CME)

Gold OTC vs. Paper Positioning*



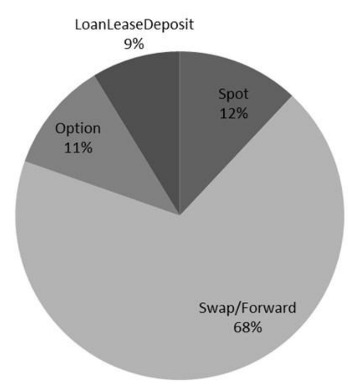
*OTC Positioning is simply aggregated reported totals across all tenors and all transaction types in LBMA-i's "open volume' report
Source: Scotiabank Commodities Strategy, LBMA-i, Bloomberg, CFTC

Gold OTC Positioning, 82bn oz, by transaction type



Source: Scotiabank Commodities Strategy, LBMA-i, Bloomberg,

Silver OTC Positioning, 1.1 bn oz, transaction type

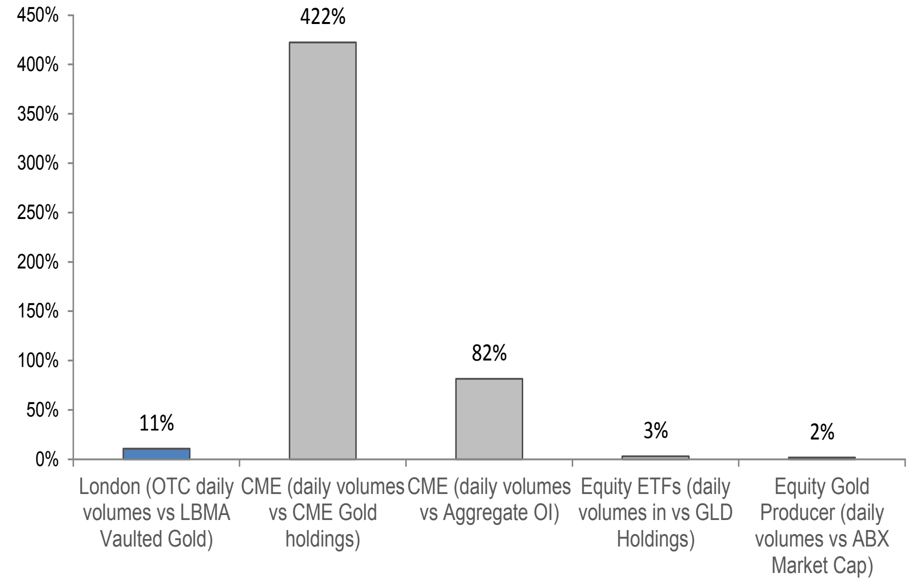


Source: Scotiabank Commodities Strategy, LBMA-i, Bloomberg,

3. Overall liquidity (or HFT gauge?) – as measured by daily volumes as a % of the "pie", positioning or metal vaulted – of the OTC Gold & Silver Market

- As of July there was ~250mn oz of Gold (and 1110m oz of Silver) in London vaults. Therefore, 26.5m oz of daily volumes only represents 11% of these holdings, but the percentage/liquidity gauge is perhaps understated since much of the allocated portion of that 250mn oz is set aside for ETFs and Gold held by the BOE on behalf of Central Banks.
- By comparison, daily volumes on CME represent 422% of the Comex Gold holdings but more accurately should be compared to the futures positioning (which represents 82% of aggregate positioning).
- GLD daily volumes only represent 3% of the total metal it holds and is closer to the daily volumes of OTC gold vs vaulted gold.
- Overall, this data drastically highlights the larger participation of systematic, HFT or intraday traders on CME and how 'financialized' exchanges have become - its pretty clear that the daily "churn" (ie: high daily volumes relative to flat or low positioning, or metal available) is highest for the NY exchanges where most of this arguably "uncommitted" activity takes place.

Current liquidity (or HFT paritciaption rate?) gauge: daily volumes as a % of either physical holdings, open positions or market cap



Source: Scotiabank Commodities Strategy, LBMA-i, Bloomberg

Other thoughts, potential outcomes & questions, and key assumptions & risks to the data:

- Its expected LBMA & LPPM will release an equivalent PGM trading & positioning report (perhaps in January 2019 when the data release changes to T+1). That would be more insightful and interesting not only because they are relatively smaller and more fundamentally driven markets, but also because of the lack of (or perceived lack?) of Palladium liquidity and volumes in Zurich.
- Gold constantly shifts between being defined as a commodity, a currency or a rates product (i.e.: unlike other commodities, it never trades at a maintained backwardation). By affirming the size of the historically unknown daily transactions, would this make Gold more susceptible to the actual availability of metal (i.e.: it trades more as commodity where forward rates are sensitive to S&Ds) or will it remain a rates/financing product contingent on the availability and liquidity of the dollar and currencies?
- The Gold market is believed to be deep and liquid (theres ~250m oz of physical gold in London vaults), but this was largely tough to gauge and measure. The reports outcomes are still early, but overtime if the OTC data conforms to these expectations and liquidity is proven, that bodes well for lobbyists aiming to reduce Golds handicap (at 50%) in relation to Basel III liquidity requirements (NSFR). Gold liquidity – and the belief that its a High Quality Liquid Asset (HQLA) – is a large and important reason why structural players (asset managers, pension funds, central banks, etc) allocate to Gold
- LBMA Volumes and OTC positioning could potentially become especially interesting around seasonal inflection points where lending is a larger feature. For example, activity and trends could be monitored around month, quarter or yearends, after theres a decent audit trail with historical data.
- Theres a potential risk that the forward market becomes “financialized” and the barrier to entry into the London forward market is lowered. Both London & NY exchanges are offering new forward market products, but there will be a key input - the availability of activity & positioning data - for any CTA, HFT or algorithmic systems to chew on and internalize.
- This service is delivered by Simplitium, which collates trades from LBMA members and publishes anonymous and aggregated trading data to the market. There are questions around some of the methodology in order to understand the data better – are swaps, options, all data netted or grossed (which implies potential double counting in the data), how are Zurich numbers known, what are the exact dates of the broad tenor dates in order to decipher between new positions or simply rolled positions, etc

Week Nov 19-23, Total Volume Report, ounces											
Product	Spot	1 Week	2 Weeks	1 Month	3 Months	6 Months	9 Months	12 Months	1 Year +	Total	%, or Average / day
Spot	72,026,545									72,026,545	63%
Swap/Forward	10,004,062	8,632,541	3,160,680	2,289,924	6,012,405	1,106,284	1,209,444	248,633	473,181	33,137,155	29%
Option	7,977	422,534	323,601	252,512	1,054,157	357,940	9,200	43,000	360,075	2,830,995	2%
LoanLeaseDeposit	1,213,563	541,619	198,250	1,899,484	1,449,311	304,776	292,755	193,688	573	6,094,019	5%
	83,252,147	9,596,694	3,682,531	4,441,920	8,515,873	1,769,000	1,511,399	485,321	833,829	114,088,714	22,817,742.80
	73%	8%	3%	4%	7%	2%	1%	0%	1%		
Spot	989,572,979									989,572,979	62%
Swap/Forward	155,618,851	104,089,851	39,195,606	83,907,650	80,050,699	19,461,737	3,230,860	935,503	5,409,103	491,899,859	31%
Option	3,601,464	1,235,402	719,157	8,824,336	35,677,863	8,658,549	1,043,800	2,641,287	5,000,000	67,401,858	4%
LoanLeaseDeposit	5,476,848	1,352,059	1,696,382	21,933,942	3,132,908			1,000,000	150,862	34,743,001	2%
	1,154,270,142	106,677,312	41,611,145	114,665,928	118,861,470	28,120,286	4,274,660	4,576,790	10,559,965	1,583,617,697	316,723,539.40
	73%	7%	3%	7%	8%	2%	0%	0%	1%		

Source: Scotiabank Commodities, LBMA-i

1234 Top 10 largest activity, or positioning

Week Nov 19-23, Open Volume (positioning) report, ounces											
Metal	Product	Spot	1 Week	2 Weeks	1 Month	3 Months	6 Months	9 Months	12 Months	1 Year +	Total
XAU	Spot	9,823,107.00									9,823,107
XAU	Swap/Forward	1,546,733.00	5,943,479.00	7,431,903.00	9,298,852.00	18,729,140.00	4,781,014.00	1,596,112.00	1,186,916.00	731,461.00	51,245,610
XAU	Option		423,868.00	694,947.00	1,359,641.00	3,236,896.00	1,671,846.00	212,550.00	416,500.00	1,127,234.00	9,143,481
XAU	LoanLeaseDeposit	223,273.00	472,075.00	440,300.00	4,410,226.00	4,392,751.00	1,227,136.00	395,298.00	193,688.00		11,754,746
		14%	8%	10%	18%	32%	9%	3%	2%	2%	81,966,944
XAG	Spot	133,481,815.00									133,481,815
XAG	Swap/Forward	29,272,546.00	65,022,481.00	82,194,139.00	287,175,697.00	224,074,318.00	53,315,937.00	11,412,857.00	2,412,051.00	7,254,271.00	762,134,296
XAG	Option		1,385,402.00	5,798,503.00	16,985,360.00	60,524,456.00	10,571,931.00	7,748,800.00	13,396,924.00	5,030,000.00	121,441,375
XAG	LoanLeaseDeposit		1,252,059.00	2,822,419.00	31,092,659.00	48,933,800.00	12,121,179.00		1,000,000.00		97,222,116
		15%	6%	8%	30%	30%	7%	2%	2%	1%	1,114,279,602