

The gold market

Products

AngloGold Ashanti's main product is gold. A small portion of its revenue is derived from the sales of silver, uranium oxide and sulphuric acid. AngloGold Ashanti sells its products on world markets.

Gold market

The gold market is relatively liquid compared with many other commodity markets. Physical demand for gold is primarily for fabrication purposes, including jewellery (which accounts for almost 80% of fabricated demand), electronics, dentistry, decorations, medals and official coins. In addition, central banks, financial institutions and private individuals buy, sell and hold gold bullion as an investment and as a store of value.

The use of gold as a store of value (a consequence of the tendency of gold to retain its value in relative terms against basic goods, and particularly in times of inflation and monetary crisis) and the large quantities of gold held for this purpose in relation to annual mine production have meant that, historically, the potential total supply of gold is far greater than demand at any one time. Thus, while current supply and demand play some part in determining the price of gold, this does not occur to the same extent with other commodities. Instead, the gold price has from time to time been significantly affected by macro-economic factors such as expectations of inflation, interest rate changes, exchange rate changes, changes in reserve policy by central banks, and by global or regional political and economic events. In times of price inflation and currency devaluation, gold is often bought as a store of value, leading to increased purchases and support for the price of gold.

Changes in exchange rates against the dollar particularly affect levels of demand for gold in non-US economies. In South East Asia, for example, during the mid-1990s strong local currencies encouraged robust gold demand due to low real gold prices in local currencies. In contrast, when South East Asian currencies fell sharply against the dollar in 1997, the local currency values of gold increased proportionally, and wholesale selling of the metal ensued in the region. Recoveries in Asian currencies since 1999 have resulted in a decline in gold prices in these currencies, which in turn has led to a rise in gold demand in Asian countries to previous levels. In the investment market, a strong dollar during the 1990s had a negative effect on investment

demand for gold in developed economies. Since 2001, the weakness in the dollar has been an encouragement to investors to buy gold.

While political and economic crises can have either a positive or negative impact on gold, this is not inevitable. As a recent example of this, in 1998, despite negative sentiment caused by the Russian financial crisis and ensuing corrections in the capital markets worldwide, the price of gold remained stable. By contrast, more recent political events in the Middle East have helped to drive the gold price higher.

The market in 2005

New levels of investor and speculator interest in gold during 2005 led to the gold price reaching 25-year highs. Despite a lull at the beginning of 2005, investor interest in gold resumed and significantly exceeded that of 2004. This was most marked towards the end of the year, the fourth year of the current rally in the gold price. The average gold price for the year was \$445 per ounce, an increase of 9% on 2004. In January 2006, the gold price reached a 25-year high of \$567 per ounce.

The weaker dollar in the first half of 2005 continued to influence the dollar gold price. However, this relationship did not apply during the second half of the year when the gold price strengthened in spite of a stronger dollar. A significant feature of the year was the break in the four-year link between the gold price and the dollar/euro exchange rate, and a material increase in the gold price in non-US dollar terms for the first time in the current gold price cycle. After averaging €325 per ounce for the past four years, the gold price reached a high of €457 per ounce on 12 December.

The resurgence in the dollar also contributed to a shift in the local currency and the rand weakened against the US dollar for most of the year. At its weakest point of R6.96/\$1, the South African currency had lost some 19% against the dollar since the beginning of January 2005, when the exchange rate reached R5.64/\$1. The rand however strengthened towards the end of the year and recouped most of its intra-year losses, averaging R6.35/\$1 for the year, compared to an average of R6.42/\$1 for 2004. The relative weakness of the rand during the second half of the year, together with the strong spot price of gold in US dollars, resulted in sharply higher rand gold prices which peaked at R111,000 per

kilogram in December, providing some relief for South African gold producers.

Several circumstances outside of currency markets encouraged interest in gold during the year. Probably the most direct influence on sentiment came from the oil market, where particularly supply disruptions caused by hurricane damage in the USA pushed the spot price of benchmark West Texas Intermediate up to a record price of \$70/barrel in early September. Speculation over the likely impact of increases in the oil price on inflation and on global economic growth led to increased buying interest in gold, and there was a correlation between increases in the gold price and the spot price of oil during the second half of the year.

Although expectations of rising inflation rates are often used to justify higher gold prices, there is little conclusive evidence of an increased threat of inflation at present, notwithstanding base metal, commodity and energy price increases in recent years. While headline inflation in the USA rose towards the end of the year, this was due largely to the impact of higher retail pump prices for gasoline, and annual core inflation in the US remains a little over 2%. Most recently, core inflation in Europe remains below 2%. Nevertheless, the impact of higher oil prices has introduced a sense of uncertainty about the health of the global economy, which continues to encourage interest in gold among both investors and speculators.

Speculative demand

To measure the extent of investor interest in the metal, the open position on the New York Comex, and the holdings of the gold exchange traded funds (ETFs) should be considered together. The Comex continued to be the most direct predictor of gold spot price movement for much of the year, with the spot price of metal tracking changes in the buying interest on that exchange until the final quarter of the year. The net open position on the Comex peaked in October 2005 at a little over the previous record level set in April 2004 of over 22 million ounces net long (685 tonnes net long), and this sustained long position on Comex has helped to keep the gold price firm and rising. To the net open Comex interest should be added aggregate investor holdings in gold ETFs, which by January 2006 amounted to some 13 million ounces or 400 tonnes of gold. These ETF holdings were accumulated mostly during the past 12 months, and predominantly from the launch of the New York Stock Exchange's

streetTRACKS fund in late 2004. The combined Comex and ETF holdings today exceed 30 million ounces, or almost 950 tonnes of gold in net investment and speculative positions in developed markets.

Demand

Physical offtake of gold continued to improve during the year. Demand fell back under the weight of the rising gold price during the final quarter of 2005, but overall figures for fabrication offtake for the year remained positive. Consumption of gold in jewellery increased by 5% for the year, largely on the back of strong growth in India and the Middle East. In India, general economic growth has translated to better demand on a wide front and during the first half of 2005, that market was able to adjust to higher and more volatile gold prices, although Indian offtake was to fall sharply during the final quarter of 2005. Improved offtake in the Middle East was sustained throughout the year, primarily on the back of increased oil revenue in that region. There was growth in demand for gold jewellery in both Turkey and China too. As has been the case for some time, however, the offtake of gold jewellery in the developed markets of the United States, Europe and Japan remained disappointing.

Net bullion supply on the market was higher, driven particularly by a year-on-year increase of over 40% in official sales of gold, to 663 tonnes for 2005, and significantly reduced de-hedging by gold producers. The market returned to an over-supply position during the second half of 2005.

With investment demand still positive for gold, the final balance of supply and demand in the gold market will remain of secondary importance. Investor and speculation purchases on the margin will continue to be the price-determining force in the gold market. However, in the longer term it is important that physical demand is healthy given the ability of the physical market to provide offtake and floor price support at times when investor or speculator interest weakens.

Official sector

The most significant issue for gold in the official sector in 2005 was the proposal made by certain members of the International Monetary Fund (IMF) during 2005, to sell outright a portion of the gold reserves of the IMF to provide debt relief for heavily indebted poor countries. While this proposal contributed to a measure of negative sentiment in the gold market at the time, the

announcement by the G8 that such a debt relief programme would not be funded by either a revaluation or sale of the gold reserves of the IMF, removed the uncertainty that IMF sales might cap the gold market in the future.

Hedging

As at 31 December 2005, the net delta hedge position of AngloGold Ashanti was 10.84 million ounces or 337 tonnes, valued at the spot price of gold on that date of \$517 per ounce. The marked-to-market value of the hedge position at this date was negative \$1.941 billion. The increase in the size and negative value of the hedge in the latter half of the year was due mainly to the increase in the spot price of gold against which the hedge is valued, which was 19% higher at the end of 2005 than the spot price of \$435 per ounce at which the hedge had been valued at 31 December 2004.

Marketing channels

Gold produced by AngloGold Ashanti's mining operations is processed to saleable form at various precious metals refineries. Once refined to a saleable product – either a large bar weighing approximately 12.5 kilograms and containing 99.5% gold, or smaller bars weighing 1.0 kilograms or less with a gold content of 99.5% and above – the metal could be sold by the refineries to the bullion banks or directly by the company to the bullion banks, and the proceeds are paid to the group.

Bullion banks are registered commercial banks that deal in gold. They participate in the gold market in buying and selling gold and distribute physical gold bullion bought from mining companies and refineries to physical offtake markets worldwide. Bullion banks hold consignment stocks in all major physical markets such as India or South East Asia and finance such consignment stocks from the margins charged by them to physical buyers, over and above the amounts paid by such banks to mining companies for the gold.

Where forward sales contracts exist against which AngloGold Ashanti delivers the physical product, the same channel of the refinery is used. In this case, the refinery does not sell the metal on the group's behalf, but instead delivers the finished gold bars to the bullion bank with which the group's forward contract is held. The physical delivery to the counterparty bank of the appropriate amount of gold fulfils AngloGold Ashanti's obligations under the forward contract, and AngloGold Ashanti is paid for this gold by the relevant

bullion bank, at the price fixed under the forward contract, rather than at the spot price of the day.

Gold market development

The challenge for marketing gold is significant. This is especially so given that demand for gold jewellery in many developed markets has declined materially in the past five years, with gold jewellery sales losing ground to other luxury consumer goods in developed markets.

AngloGold Ashanti is committed to growing the market for gold. The group's marketing programme aims to increase the desirability of its product, to sustain and grow demand, and to support the deregulation of the market in key economies.

During 2005, AngloGold Ashanti spent some \$13 million on gold marketing initiatives, of which 66% was spent through the World Gold Council (WGC). Gold marketing expenditure by AngloGold Ashanti in 2004 and 2003 amounted to \$15 million and \$19 million, respectively.

Independently of its support for the WGC, AngloGold Ashanti is active in a number of other marketing projects that support gold. It remains the only gold group in the world to have committed this level of resources to the marketing of the metal it produces.

Downstream initiatives have included GoldAvenue, an internet venture selling gold jewellery, established between AngloGold Ashanti, JP Morgan Chase and Pamp MKS of Geneva in 2000. This venture continued to sell gold jewellery by catalogue and website until early 2004, after which it was wound up.

The United States remains an important focus market for AngloGold Ashanti's marketing initiatives, due to its value and influence on gold jewellery retailing trends. However, AngloGold Ashanti now includes in its international marketing initiatives the emerging markets of India and China. In both of these markets, gold jewellery purchases have a traditional or cultural motivation. Among modern urban consumers in India and China, however, gold jewellery is increasingly competing for consumer spend with other luxury goods. Initiatives in India and China therefore focus on the modernisation of retail channels for gold jewellery consumption and on the development of a modern product offer which can sustain and grow consumer interest in gold jewellery purchases for non-traditional reasons.

AngloGold Ashanti holds a 25% stake in OroAfrica, the largest manufacturer of gold jewellery in South Africa, as an investment in the downstream beneficiation of gold in South Africa. AngloGold Ashanti and OroAfrica have co-operated in a number of projects, including OroAfrica's development and launch of an African gold jewellery brand. An important strategic step has been the establishment of a Jewellery Design Centre at OroAfrica at a cost of \$250,000. The purpose of the Centre is to generate new gold jewellery designs, and to improve product standards through technology, design and innovation. The Centre has been used during the past year to develop a new range of gold jewellery with an African theme. The Design Centre was commissioned by the South African Parliament in 2003 to manage the fabrication of the new Parliamentary mace to celebrate the tenth year of democracy in South Africa. The mace was successfully completed and presented to Parliament in 2003.

Also in the area of design innovation, AngloGold Ashanti's Riches of Africa Gold Jewellery Design Competition was established in 1998 to showcase South African jewellery designers, to enhance jewellery manufacturing technical skills in South Africa, and to support the local gold jewellery industry. Training workshops for competition entrants are held each year, while the award-winning works are exhibited and used in fashion shows and other events both locally and abroad. The 2005 competition attracted a record total of 559 entrants and a record number of student and professional jewellers attended training workshops held by AngloGold Ashanti in Johannesburg, Cape Town and Durban.

A biennial gold jewellery design competition in Brazil, the Designers Forum, was launched by the group in 2002. It was the first such competition in that country. The competition generated unprecedented interest in 2004, with a high quality of design and craftsmanship and some 650 projects involved. From these, 33 pieces were selected for the collection.

The Gold of Africa Museum was inaugurated in 2001 in Cape Town with the permanent endowment of the Barbier Mueller collection of West African gold objects purchased by the company in 1998. The museum also serves as a training facility in the jewellery industry in Cape Town. The museum continues to attract a growing number of visitors, and to provide special visits for school groups in the Cape Town area.

Other South African projects in 2005 include the launch of a scheme to provide cost-effective financing for South African gold jewellery manufacturers, in partnership with Gold Fields Limited, BAE Systems/Saab (through defence contract offset obligations) and Standard Bank. The scheme aims to lower the cost of financing gold working inventory to manufacturers, thereby enabling them to compete more effectively in international markets. In 2005, AngloGold Ashanti also worked in conjunction with the Department of Trade and Industry (DTI), the Industrial Development Corporation of South Africa (IDC) and the WGC to produce a publication on the gold industry in South Africa entitled 'Gold in South Africa: Mining, Refining, Fabrication and Trade'. This publication is intended to provide a source of reference on the gold industry in South Africa and is the first attempt to collate data on the South African gold industry in all of its various activities.

AngloGold Ashanti and Mintek, South Africa's national metallurgical research organisation, launched Project AuTEK in 2002 to research and develop industrial applications for gold. Project AuTEK has developed a gold-based catalyst for the oxidation of carbon monoxide at ambient temperatures. Mintek has carried out pilot-scale catalyst production tests. Negotiations for the commercial production of the catalyst have commenced.

An important feature in many of AngloGold Ashanti's marketing projects has been the beneficiation of gold, particularly in South Africa. AngloGold Ashanti's commitment to adding value to gold extends beyond mining and aims to contribute towards the upliftment of people and the sustainability of communities.

AngloGold Ashanti remains a sponsor of the Atteridgeville Jewellery Project, established in 2000 by the Vukani Ubuntu Community Development Project to create opportunities in the jewellery industry in South Africa for the previously disadvantaged through training and development. In 2004, the company also sponsored the expansion of the Soweto Jewellery School to enable it to double its intake of students from 2005.