International Journal of Academic Research
ISSN: 2348-7666; Vol.3, Issue-8(1), August, 2016
Impact Factor: 3.656; Email: drtvramana@yahoo.co.in

New Experiments with Gold Schemes

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Abstract: *The costly product which do not earn even a single pie and which has the highest demand among Indians that is only gold. For Indians, especially for women-folk, gold is an attractive and much desired metal. No country in the world except China possesses as much gold as India has which is named as poor country. Meanwhile, the Centre of late has come out with three new gold schemes Viz Gold Coin and Bullion Scheme, Sovereign Gold Bond Scheme, and Gold Monetisation Scheme. There is a dire need to discourage public to purchase physical gold and to show alternative avenues for investing their money in paper gold. The recent introduction of above three gold schemes is a step in correct direction.*

Keywords: *Gold, women-folk, gold imports*

Introduction

The costly product which do not earn even a single pie and which has the highest demand among Indians that is only gold. For Indians, especially for women-folk, gold is an attractive and much desired metal. Of late, India emerged as the highest consumer among the countries in the world. It is this consumption which is overturning our economy. Barring two years, in all other years our foreign trade has been witnessing deficit. That means our imports transgressed our exports. Indian gold imports occupied third place next to crude oil, and Machinery. The latter two items contribute to the economic development while the former constitutes an unproductive asset. Of late Modi in his latest "Man Ki Bat" radio programme, named gold as "dead money". It is ironical that rich, middle and even poor households spend huge sums on such idle asset resulting in huge imports of gold leading to trade deficit every year.

Circumstances forcing to introduce gold schemes: The Centre of late has come out with three new gold schemes Viz Gold Coin and Bullion Scheme, Sovereign Gold Bond Scheme, and Gold Monetisation Scheme. There are two reasons for the introduction of these schemes by the Indian Government. First the ever increasing household demand for yellow metal resulting in heavy dependence in gold imports. Apart from this, every year, for purely investment purpose, jewellery traders used to import 300 tonnes. Second, an estimated 20,000 tonnes of gold worth Rs. 5, 40,000 crores is lying idle in the private vaults and bank lockers.

Curbing the gold imports: - The yellow metal constitutes a third of the country's entire imports. The surge in gold imports was very steep. In 2005-06 gold imports were less than \$11billion, but within the next six years, its imports had increased to nearly \$ 57 billion which constitutes around 12 per cent of the total import bill. Gold has taken the place of "Machinery group" whose share of imports fell from 18 per cent in 2007-08, to 10.6 per cent in 2012-13. Surprisingly, gold imports plunged to fourth place (6.4 per cent) next to electronic goods (6.9 per cent). In 2013-14 Gold imports declined by huge $ 43.3 billion in that year. The sharp decline in gold imports in 2013-14 was mainly due to policy initiatives that sequentially hiked the duty on gold over a one-and-a-half year period as well as imposed quantitative restrictions on gold imports.

As regard the duty on gold is concerned, the Union Budget 2012-13 had increased the basic customs duty on standard gold from 2 per cent to 4 per cent. Subsequently the duty was increased to 6 per cent on 21st January 2013 and thereafter to 8 per cent on 5th June 2013 and finally to 10 per cent on 13th August 2013. Coming to the quantitative restrictions in July 2013, banks and other jewellery trading export houses were not allowed to import gold and only 10 designated banks and other agencies and entities could import gold under the 80:20 rule which means that at least one-fifth of every log of gold imports had to be made available for exports and the balance for domestic use. It is apparent that the speculative demand for gold was brought under control only when import duty touched 8 per cent and these quantitative restrictions were put in place. The impact of these two steps on gold imports was dramatic. During 2013-14, the value of gold imports was $29 billion accounting for more than 46 per cent decline as compared to the immediate previous fiscal year. However, the world Gold Council in its report pointed out that the underlying level of demand for gold among Indian consumers had remained strong during 2013-14. The report concludes that “the sharp decline in the official import of gold into India led to an increasing amount of this demand being met by gold imports through smuggling. Whether gold imports are official or unofficial, there would be a drain on our valuable foreign exchange. So these two measures met with limited success.

In absolute figures, our gold imports have gone up form Rs. 18,608 crores to Rs. 47,951 crores in 2005-06. By 2011-12 they reached to an unimaginable figure of Rs. 2.28 lakh crores and occupied second place as mentioned above in our total exports contribution to the surge in the trade deficit to an alarming figure of 10.2 per cent and Current Account Deficit to 4.5 per cent. This resulted in weakening our currency to that extent in the international market. India imported Rs. 2.1 lakh crore worth of gold in the financial year 2014-15 not counting jewellery. So far Rs. 1.12 lakh crore worth of gold has been imported between April-September 2015. Time has come to curtail the gold imports which occupy one-third of our total country exports. Towards this end, there is a dire need to discourage public to purchase physical gold and to show alternative avenues for investing their money in paper gold. The recent introduction of above three gold schemes is a step in correct direction.

Converting idle gold into ideal investment:- In our country as mentioned already an estimated quantity of 20,000 tonnes of gold is lying idle in the households and temples. The Government aims to mobiles at least part of this idle gold and use it for productive and welfare purposes. India being the largest importer of gold in the world with annual gold imports around 800 tonnes, the government can minimize imports by using domestic gold for productive purpose.

Sovereign Gold Bond Scheme:

These bonds are available from banks and designated post offices. Under this scheme, the investor or consumer instead of buying gold in physical form buys a paper gold bond with that money. These bonds will be denominated in multiples of gram(s) of gold amount. With a basic unit of one gram with a minimum tenor of 8 years with a minimum lock in of 5 years, so that they would protect investors from medium volatility in the gold prices. The buyers buying bonds will not be allowed o purchase less than two grams worth bonds and not more than 500 grams worth per person in financial year. At the time of redemption by the depositor, if there is an upward increase of gold rates it would be a loss to the government but a gain to the bond holder. The reverse is the case if there is a decline in the gold rates. The investor also gets interest at the rate of 2.75 per cent (fixed rate) per annum on the initial investment. Interest will be credited semi-annually to the bank account of the investor and the final interest will be payable on maturity along with the principal. This scheme is a good idea and could be a success. It primarily targets the present investing community accounting about 300 tons a year which purchase gold only for investment purpose. These bonds will also be tradable on exchanges if held in demat form. It can also be transferred to any other eligible investor.

A separate fund will be created out of the sale proceeds of these bonds. Any risk arising from increase in gold rates in the future would be met from this fund. The success of this scheme from the government point of view will depend on successful investment of amounts accumulated in this fund. If the fund is kept idle or invested in speculative investments or lend to private corporate people with bad track record the scheme will turn into a fiasco, the reason being the owners of these bonds are bound to be paid interest for the actual period of the bond. Moreover, if there is an increase in the international gold prices in future, the government has to bear that unforeseen loss. To overcome these contingencies, it is better if the fund is utilized for lending to State Governments or Government units, or local self-governing bodies for which there is no possibility of bad debts. There are two points to be kept in mind. First we cannot expect the poor and lower middle class people to buy these bonds as their discretionary income are almost zero. These people whenever they purchase gold they purchase gold only at the time of marriages. For these people especially villagers gold sentiment is much more and they would not prefer paper bond to physical gold. Moreover Indians especially the above category of people purchases gold for making ornaments to be used at the time of auspicious occasions. If they purchase bonds, they would not serve this emotional purpose. Such people view at gold linked to tradition and customs rather than as a mere investment asset. Secondly the scheme attracts the “black” or unaccounted money possessed by most individuals. It gives scope for such people to invest their black money with benami names of their Kith and Kin every year, thus converting their black money into white money.

Gold Monetization Scheme:

It is a misnomer to call India a poor country as it has 20,000tonnes of gold lying in households and temples. The main purpose or gold deposit scheme is to make this domestically available gold to put to productive use. The depositor under this scheme will deposit his gold like a fixed deposit with a minimum tenure of 1 year. The minimum deposit at any one time shall be raw gold equivalent to 30 grams of gold of 995 purity. There is however no maximum limit for deposits under the scheme. The depositor as in the case of fixed deposit will get deposit certificate from the bank and the principal and interest of the deposit under the scheme will be determined in gold. The terms of deposit vary from short-term deposits (1-3 years), medium-term deposits (5-7 years) and long-term deposits (12-15 years). The interest rates have been fixed at 2-25 per cent to 2-5 per cent on these deposits to ensure the schemes success. The new scheme is almost akin to Gold Deposit Scheme introduced in 199. The important difference between the two is the minimum quantity of gold than can be deposited which is 30 grams as against 500 grams under the Gold Deposit Scheme. The underlying objective for fixing such a low quantity of gold as minimum limit is to involve some institutions and households rather than temples and trusts.

There are four benefits to the depositors of gold under this scheme. They are 1) fixed interest on the value of gold deposited 2) ensuring security to the gold which is absence if it is kept in the house. 3) Savings in the locker charges if it is already kept in the bank locker and 4) Benefitting the depositor who benefit if the value of gold appreciates at the time of redemption. On the other hand there are four issues which prevent the depositor to deposit their gold under this scheme.

1) Under this scheme the depositor has to specify in the beginning whether he/she wants to redeem it in cash or gold. Even if it is in gold it will be standardised gold bars. The bank will not return the same ornaments which he has deposited instead he gets melted pure gold of equal weight. 2) The female-members in the family of the depositor will not find gold ornaments to wear during auspicious occasions if he deposits the entire gold in the bank. Even if it is partly deposited, they are prevented to wear gold ornaments to that extent during such occasions. The Indian women emotionally feel that if she wears more ornaments during such occasions, she would get more respect and status from her counterparts. 3) A depositor will not part with gold if he inherits the same from his grand ancestors, because he will not get back the same gold at the time of redemption. It would be unwise to expect families especially from rural areas to actively involved in any scheme that involve "melting" is age long – preserved ornaments. The past record of the gold deposit schemes is a testimony to this as the response from the public was insignificant. For example SBI gold scheme 1999 through in existence for 25 years, has attracted only about 8 tonnes so far. The same household sentiment applies even temples trusts as the gold lying in temple coffers are linked to faith and religion. The donors now-a-days also expect the gold jewellery they have donated to the temples should be as it is and their sentiments will be affected if it is melted. 4) In case the price of gold drastically falls at the time redemption, the depositor will be the looser.

From the Government point of views there are three challenges:

1)If the bank faces an adverse situation wherein large number of depositors withdraw their deposits at a time and if the bank does not possess enough gold, it has no alternative except to import gold on large scale which may result in trade deficit. 2) In case there is no demand for the deposited melted gold from gold traders it will remain idle in the bank coffers making it difficult for the bank to pay interest to the depositors. 3) The scheme encourages hoarders of black money to purchase large quantities of gold with the black money lying with them and deposit them with banks, thus facilitating the conversion of black money into white. Those who possess unaccounted wealth stored in the shape of gold ornaments and bars will find this as an excellent opportunity to legitimize their ill-gotten wealth. Since there is no documentation required for the purchase, it will be difficult to verify the ownership of the gold deposited under this scheme. Of course, such transactions are subject to KYC norms.

Conclusion: No country in the world except China possesses as much gold as India has which is named as poor country. In the words of our Prime Minister Modi it is dead money which should be converted into living force by depositing it in banks. In his recent Man Ki Bath radio broadcast, he further pointed out that unproductive gold lying in India is a source of economic strength for the country if every Indian should contribute to making it the country prized economic asset. As mentioned above India every year imports 800 tons of gold if the Government succeeds in bringing back at least 5 per cent of the unproductive 20000 tonnes of gold into the purview of this scheme every there is no need for the country to depend on imports. Since future prices of gold are likes to be higher than the present ones, it would be advisable if the middle class households invest their saving for the future marriages and education of their girl-children. Since most of the temples are under the control of the respective State Governments, the Centre can convince the latter to deposit the vast gold lying with temples and trusts in Gold Monetisation Scheme. A few years back the TTD has come forward to deposit large quantity of its gold under Gold Deposit Scheme 1999. Unfortunately the biggest constraint the Government confronts is the right perception and attitude of the consumers towards gold. The 2.25-2.5 rate of interest is an attractive offer to get some return on their gold for those with unused yellow metal and seek to use this for investment. In view of the poor response to these schemes, the Government may think of extending the time for some more days. To what extent these schemes will be successful time alone will prove.

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