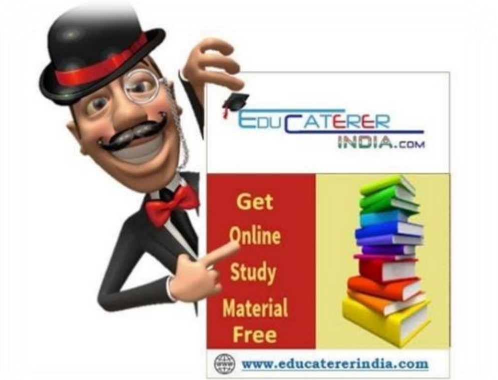
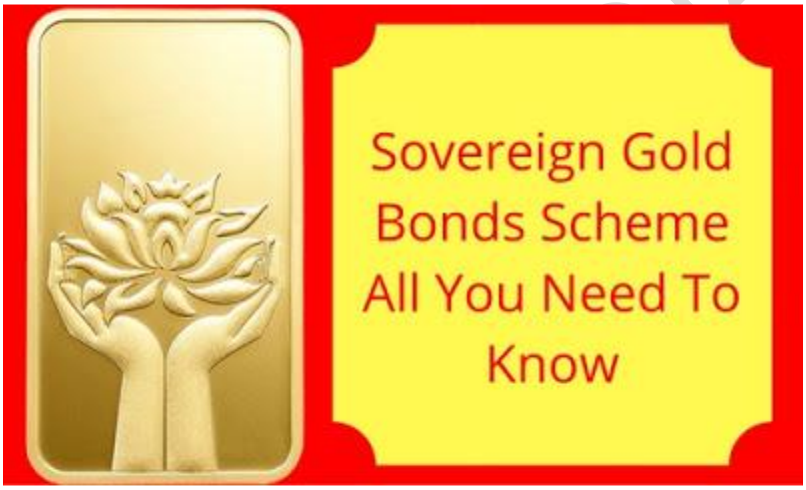
UNIT 6 - Sovereign Gold Bonds Scheme- All You Need To Know





Introduction

Sovereign Gold Bonds scheme was launched in the budget session 2016 and approved by the cabinet to reduce the demand for physical gold

Background

- India is one of the largest importers of Gold in the world
- The demand for Gold in India is rising rapidly
- Imports of India see a hike with Gold as the major contributor
- This affects the balance of trade figures for India
- GOI needed to restrict the Gold imports to have a positive balance of trade
- This created the need for Gold bonds scheme
- Gold Bonds are seen as an alternative to purchase gold metal

About Gold Bonds

- Gold Bonds are issued by RBI with a fixed interest rate
- Ministry of Finance is the concerned ministry
- RBI in consultation with Finance ministry determines the issuing amount
- Risk of gold price changes borne by the Gold Reserve Fund created by RBI
- GOI aims to shift 300 tonnes of Gold purchased annually as bars and coins into the Gold Bond Scheme
- This Gold Bond scheme is expected to help GOI sustain the current account deficit

How does Gold Bonds Work?

- Gold Bonds are sold in banks
- Investor can walk in buy the gold bonds from the banks preferably where they have their Saving Bank accounts
- Gold Bonds are treated in a similar manner as a Bank Fixed Deposit
- The interest rates are fixed at 1 to 2 percent
- The tenure of the bond is from 5 to 7 years
- Value of the bond is determined by the gold price movements in the market
- Gold Bonds have an attractive feature
- The investor will get the value of bond according to the prevailing gold prices in the market at the time of redemption
- In this manner, the investor will get the same benefit of purchasing the metal gold without actually purchasing it
- In this manner, GOI can restrict Gold imports to a certain extent
- Returns on gold bonds can be positive or negative
- All risks of the gold bond are covered under the Gold Reserve Fund

Features of Gold Bond

- Bonds issued by RBI with a sovereign guarantee
- Bonds can be easily traded and sold on exchanges
- Gold Reserve Fund will be created by GOI through RBI
- On gold bond maturity, redemption will be made in Rupee only
- Price of gold bond will vary with the market prices of gold

- Investor needs to be aware of this price volatility
- Gold bond deposits will not be hedged
- RBI has fixed tenor of the bond from 5 to 7 years to protect the investors from medium term volatility

Limitations

- NRI cannot buy gold bonds issued by RBI
- Common Indian buys gold for marriage and other occasions as a Jewellery and not for investment purpose
- The attitude of a common Indian towards gold is not of investor nature
- This attitude will see a Luke warm response to the Gold bonds scheme
- Also, the interest rate offered is very low in the tune of 1% to 2%

Conclusion

- The effectiveness of the scheme will depend on the investor attitude towards the gold bond scheme
- GOI must take steps to change the mindset of Indians from viewing gold as a jewellery or a status symbol to an investment avenue
- This transition in behaviour of Indians will take time
- Overall, Gold bond scheme is a welcome measure to cut imports on gold purchase