

# IMPACT OF GOLD TRADE ON INDIAN ECONOMY

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## ABSTRACT

Since gold policies play an important role in macroeconomic approach of economic policies in India, it is essential to study their impact on the gold demand. The market has seen a change in the trend in strategy, that is, from various limitations to an entirely changed gold market. It's the arrangement approach that decides whether gold is still profitable or it has become an ineffective source. While incorporating gold market sector with finance related sectors, this changed or modified gold market has provided a great concern for the buyers, leading to the growth of gold market. This study will examine the impact of various government policies on the gold market, including the import as well as export of gold.

**Keywords:** Gold, India, Imports, Government Policies

## INTRODUCTION

In the Indian connection, money related, monetary and budgetary segment arrangements have assumed a noteworthy part in affecting the ways of financial development, inflation, interest rates, exchange rate and asset prices, which serve as key drivers of gold demand. Until 1991, India's macroeconomic arrangement environment was portrayed, extensively, with monetary strength and financial repression, inferable from the target of minimizing interest cost to the central bank, inflexibility in the bank rate, the policy rate at which national bank loans to government, statutory pre-emption of banks and credit. There existed capital inflow restrictions and the external sector remained closed. The exchange rate was pegged to a basket of currencies to improve exports and abridge imports. With the dominance of public sector banks the monetary system lacked ideas. Deposits and government securities stayed as the major equipments of financial savings. Even though the equity and insurance market existed they required growth momentum. After the new liberalization policy began in the 1990s the economy witnessed the authority of banks to set interest rates. A critical issue which arises is whether the changes in monetary, fiscal and financial policies under reforms have significantly influenced India's gold demand, to know that the various gold policies adopted by the government are discussed. India has traditionally been the largest consumer of gold in the world and the

government has adopted a range of measures to manage this consumption. The policy initiatives in India over the past six decades is studied.

## OBJECTIVES

1. To study about the various government policies laid on the gold market.
2. To understand the impact of the government policies on the gold market

## GOLD IMPORT SCHEMES AND GOVERNMENT POLICIES IN INDIA

The Indian government's interest in the gold market dates back to independence. In order to better understand the differing approaches taken and their respective consequences, the policies from 1947 to present is assessed.

Table I  
**Gold Price History for the Last 50 Years for 10 gm (24k)**

Year	Price (₹)	Year	Price (₹)
1964	63.25	1989	3140
1965	71.75	1990	3200
1966	83.75	1991	3466
1967	102.50	1992	4334
1968	162.00	1993	4140
1969	176.00	1994	4598
1970	184.50	1995	4680
1971	193.00	1996	5160
1972	202.00	1997	4725
1973	278.50	1998	4045
1974	506	1999	4234
1975	540	2000	4400
1976	432	2001	4300
1977	486	2002	4990
1978	685	2003	5600
1979	937	2004	5850
1980	1330	2005	7000
1981	1800	2006	8400
1982	1645	2007	10,800
1983	1800	2008	12,500
1984	1970	2009	14,500
1985	2130	2010	18,500
1986	2140	2011	26,400
1987	2570	2012	31,050
1988	3130	2013	29,600

Source: [www.goldprice.in](http://www.goldprice.in)

## PHASE ONE (1947 TO 1963)

Foreign Exchange Regulation Act: Before the independence the internal price for gold was only Rs 21 per 10 grams while the international price was Rs 34 per 10 grams. Naturally it was profitable to export gold. The traditional demand for gold was savings demand and not speculative demand. In India the huge and increasing demand for gold led to the policy of refusing gold import licensing. Since licenses were not

introduced, gold was mainly brought by illegal transit or smuggling. The preclusion on the import of gold existed in India since the time of independence from 1947. Amid the first stage, 1947-1962, approaches were generally equipped towards controlling the gold market in India. The Imports and Exports (Control) Act was enacted in 25th March 1947. Estimates show that during 1948-49 around 27.36 tonnes of gold was smuggled to India. It increased to 35.35 tonnes in 1950-51 and to 53.27 tonnes in 1952-53. There was more than 50 percent decline in the gold smuggled during 1955-56 and fell down to 26.27 tonnes. This reduction in 1955 was due to the measures undertaken by the government in the annual budget 1953-54 to arrest the drain in gold reserves, and as a result the drain was halted to a certain extent. In this period the Indian government had banned gold imports and then later brought in a new licensing system. Neither had the coveted impact, and rather saw the growing of illegal carrying rings. The consequence of the world war two led to the arousal of such an act. The act was started basically for three years but it was updated from time to time till 1971. Initial life of the Act was three years but it was extended from time to time till 1971. The main intention behind such a restrictive approach to gold was, to detach people from gold, to manage the gold supply in the country, to reduce smuggling, to bring down the demand for gold and to decrease the domestic price of gold. In 1947 the price of gold was Rs 88.62/10gms. After the announcement of the act there was not reduction in the price. Price of gold increased to Rs95.87/10gms in 1949 and dipped to Rs 79.18/10gms in 1955.

**Kolar Gold Mining Acquisition Act:** Another notable event in this phase is the nationalization of the Kolar Gold Mines. In spite of production more than 95 percents of India's gold output annually the mines started declining; hence they were nationalized and handed over to the government to prevent closure. In 1958 the government tried to retain the domestic output from the mine as unofficial reserves. The price of gold was Rs 90.81 per 10 grams and reached Rs 97 per 10 grams in 1963. Around 520 tonnes of gold was unofficially imported between 1958 and 1963.

**Gold control act:** The steep increase in gold price at Rs 119.75/10 gms and uncontrolled smuggling compelled the then finance minister Morarji Desai to propose the Gold Control Act, 1962, which canned all gold loans given by the banks and banned future trading in gold. The gold bond for 15 years was issued in exchange of gold bars and coins. The government urged the public to refrain from purchasing gold and surrender their holdings.

**Gold control rules:** the rule in 1963 promulgated to impose severe restrictions on the gold market. Gold jewelry above 14 carat was banned. Government tried to exercise control over domestic trade and gold distribution was firmly established. The price of gold descended to Rs 63.25 per 10 grams. The result was that the demand for gold remained strong as ever and gold smuggling became the order of the agenda. Smuggling of gold accounted to 30-70 percent of actual imports. The hawala market flourished to pay for the smuggled gold through remittances.

## PHASE TWO (1964 TO 1989)

A restrictive approach persisted between 1964 and 1989. National Defense Gold Bonds: The Government of India had issued a bond in 1965 which redeemable after 15 years, that was, after 1980. This was launched with the benefit of tax immunity for unaccounted holdings. The smuggled gold amounted to 720 tonnes between 1964 to 1967. But the newly launched steps failed to yield the expected results. The price of gold also increased to Rs 102.50 per 10 grams in 1967.

**Defense of India Rules:** The rule was introduced in 1966. Fabrication of jewelry above fourteen carat was permitted, but the personal possession of gold bars and coins were banned. Specified limits of the gold jewellery had to be declared by the owners. Rigid control over gold refineries was made with a target to bring gold refineries under the government authority.

**Gem and Jewellery Export Council:** The gem and jewelry export council was also established during 1966. The main vision was to main India the source of quality gems and jewelry.

**Bharat Gold Mines Limited:** In 1972 the BGML was built up by the administration of India under the Ministry of Mines and the Kolar mines were given over to the BGML to be kept running as open segment undertaking of the central government.

**Voluntary disclosure of Income and Wealth Ordinance:** The administration attempted to activate gold by issuing gold bonds and gold auction plans through the Voluntary Disclosure of Income and Wealth.

**Gold Auctions:** An auction sale was conducted by the government in 1978 between April and October. The sale was made to the certified goldsmiths and licensed dealers. Around 13 tonnes of gold was sold. The price of gold was Rs 685 per 10 grams and 210 tonnes of gold arrived unofficially to the country during 1974 to 1978.

## PHASE THREE (1990 TO 2006)

Between 1990 and 2006, a different approach was adopted as the government introduced measures to deregulate the gold industry. By 1985, India had begun having balance of payment issues. Before the end of 1990, India was in a genuine financial crisis. The government was near default, its central bank had denied new credit and foreign exchange reserves had been lessened to such a point, to the point that India could scarcely back three weeks of imports which drove the Indian government to transit national gold reserves as a promise to the International Monetary Fund (IMF) in return for an advance to cover equalization of balance of payment obligations.

Table II  
**Relationship between Gold Price Growth and Inflation**

Year	Price (₹)	Average gold price growth (per cent)	Average inflation rate	Average inflation growth rate (per cent)
2001	4300	-2.33	3.77	9.13
2002	4990	16.05	4.31	14.32
2003	5600	12.22	3.81	-11.60
2004	5850	4.47	3.77	-1.05
2005	7000	16.43	4.25	12.73
2006	8400	16.67	5.79	36.24
2007	10,800	28.57	6.39	10.36
2008	12,500	15.74	8.32	30.20
2009	14,500	16.00	10.83	30.16
2010	18,500	27.59	12.11	11.81
2011	26,400	42.70	8.87	-26.75
2012	31,050	17.61	9.30	4.85
2013	29,600	-4.67	11.05	18.82

Source: [www.inflation.eu](http://www.inflation.eu)

**Repeal of Gold Control Act:** This ordinance was set up in 1990. The domestic trade was deregulated. Merchants, fabricators, retailers and refiners could work without requirement for licenses. Confinements on the private responsibility of gold were uprooted. In any case, at this stage, there was no approach to encourage the official import of gold. The price of gold was Rs 3200 per ten grams and the consumer demand for gold in the country accounted to 178 tonnes. 176 tonnes of gold arrived through the official channels. About 5596kgs of gold was smuggled during the year.

**Liberalization:** The economic liberalization was instituted in 1991, with an aspiration of preparing the economy more market-oriented and developing the role of private and foreign investment. Definitive changes include a minimization in import tariffs, deregulation of markets, contraction of taxes, and larger foreign investment.

**Non-resident Indian scheme:** The NRI scheme was presented in 1992, along with a Special Import License (SIL) which was extended to incorporate gold as an import commodity in April 1994. These plans were to encourage opening of gold into India. But this scheme only increased the consumer demand for gold from 157 tonnes in 1991 to 264 tonnes in 1992. The price of gold also increased from Rs 3466 to Rs 4334 per 10 grams in 1991 and 1992 respectively. With the modified import license the gold import through official channel was 262 tonnes. This helped in reducing the illegal gold purchase to 2889 kgs in 1992, which was 4946 kgs in 1991. The new policies helped to reduce smuggling to a great extent. The year 1993 and 1994 was followed with further declines in the smuggled gold. It crashed to 1372 kgs and 1147 kgs in 1993 and 1994.

**Bank authorization:** In 1997, The Reserve Bank of India approved seven banks to go about as offices for import of gold, silver and platinum, in particular the Bank of India, Allahabad Bank, Indian Overseas Bank, Canara Bank, ABN-Amro Bank, Bank of Nova Scotia, and Standard Chartered Bank. With new banks

operating official imports increased to 642 tonnes in 1997. The consumer demand for gold was 675 tonnes in the same year. The price declined from Rs 5160 per 10 grams in 1996 to Rs 4725 per 10 grams in 1997. The illegal arrival of gold was computed to 1325 kg.

**Gold deposit scheme:** In September 1999, the Government of India dispatched a Gold Deposit Scheme to use the unmoving gold and at the same time give a gain to gold owners and lessen the nation's dependence on imports. The administration attempted to activate gold through the Gold Deposit Scheme (GDS), dispatched by State Bank of India to permit gold reserves at a predetermined interest rate. In any case, this arrangement was not generally acknowledged by the populace. The total consumer demand for gold was 654 tonnes for the year 1999. The price of 10 grams of gold was Rs 4234 and around 651 tonnes of gold was imported through official channels. Between 2000 and 2006 government did not initiate any strict import policies. This helped the government to an extent to reduce the smuggling. But the year 2004 marked a shocking figure of 225.99 crores worth of gold smuggling which was only 10.04 crores worth gold in 2003. About 70.40 percent increase in smuggling was seen in all sections during 2004. Further the officials were successful in controlling and the preceding year marked an amount of Rs 1.14 crores of gold smuggling which again dripped to Rs 0.28 crores in 2006.

#### **PHASE FOUR (2007 TO PRESENT)**

The period amidst 2007 and 2009 has been the most tumultuous in monetary market's late history as the world economy dove into 'great Recession'. It brought about banks breakdown, equity markets tumbled over the globe, exchange contracted, capital flows became scarce, development drooped and credit spreads heightened sending speculators escaping for the front of conventional place of refuge resources, for example, government securities and gold. Most outstandingly, the novel component of the Recession was that, it for all intents and purposes put even the long trusted monetary establishments, to corrosive test on their fitness of liquid portfolio administration. Also, conveyed to the fore the phenomenal weakness of the global financial system to interruptions in wholesale funding markets. Indeed, even extremely old financial institutions were lessened to rubble. The fourth phase started in 2007, just ahead of the global financial crisis. This phase has been pronounced by ascending gold demand, increasing imports, rising prices and a huge current account deficit.

**Gold ETFs:** They started functioning in India from March 2007. Gold exchange-traded products are exchangetraded funds (ETFs), closed-end funds (CEFs) and exchange-traded notes (ETNs) that intent to trail the price of gold. In 2007, consumer demand for gold totalled 773 tonnes. At the same time, the gold price was Rs 10800 per ten grams.

**Foreign trade policy:** The trade policy for the year 2009-2014 was introduced in 2009. The main objective of the policy was to double the percentage share of international trade within five years and to act as a

powerful equipment of economic growth by giving an upshot to employment. Fortunately, or unfortunately this period, witness a high growth in consumer demand, gold price, smuggling and importing. The trade policy did not prove much effective to the behavior of the Indian consumers towards gold. The price of gold which was Rs 10800 in 2007 peaked at Rs 29236 per 10 grams in 2013. The demand also remained around 900-1000 tonnes from 2010- 2014. To try and cutback the current account deficit and bring down the depreciation of the rupee, the government started introducing restrictions on the gold market.

**Import restrictions:** The year 2013 was unforgettable in the history of India. The government could not control the public consumption or the price of gold. The price of gold reached its zenith level of Rs 29236 per 10 grams along with an increase in the consumer demand at 974 tonnes. The current account deficit was warded intractably. The government had to impose import duty for around five times in one single year. On 21st January 2013 Indian import duty on gold was raised from 2 percent to 4 percent, which soon raised to 6 percent in short span. Surprisingly they were successful in dipping the gold imports to 215 tonnes in January to March. But in April to June the gold imports again jumped to 336 tonnes. Before lingering for long the Indian import duty on gold again raised from 6 percent to 8 percent on June 5th 2013. This helped to bring down the gold imports to 31.5 tonnes on monthly basis. On 13th August 2013 once again, the Indian import duty on gold was increased from 8 percent to 10 percent. But after the initial effects of the restrictions fade away the consumers soon get used to the new price and start to consume and import more. Finally, the government had to increase the import duty from 10 per cent to 15 per cent September. The most devilish side of this import charges was reflected in the form of smuggling. The year 2013 marked an Rs 173.42 crore worth of recorded gold smuggling where as there are many unrecorded cases.

On 28th November 2014 when the new government sworn into the office on 26th May 2014 the Reserve Bank of India announced the removal of the 80:20 import restrictions with immediate effect. The 2015 budget presented by Arun Jaitley on 28th February 2015 announced three gold policy measures; Gold Monetisation Scheme, Sovereign Gold Bond and an Indian Gold Coin

**1) Gold deposit scheme:** This scheme is expected to function identically like the bank account. In case of bank account individuals receive interest for their deposit. Similarly, this scheme will provide interest to the households and jewelers for the gold deposit they make with the bank. The bank will also lend the deposited gold to the jewelers who require gold for their daily business purpose. The scheme was introduced with a vision of two prolonged benefit, firstly it will help to reduce gold imports. Secondly, the gold that is unproductively stashed away in house hold lockers can be brought into circulation. This will save the country's billions of rupees annually. Poor marketing by the government for its gold monetisation scheme (GMS), sovereign gold bond and Indian gold coin scheme is why these have had poor public responses, says the India Gold Policy Centre (IGPC) at the Indian Institute of Management here (IIM-A).

**2) Sovereign Gold Bond:** The sovereign gold bond is exactly like other bonds. Under this bond, the Government issues these bonds to borrow the money for the numerous activities. The government will receive money from investors who invest in the bond and in turn pay a fixed periodic interest. After the time lapse the money is returned to the investors. Similarly, in a gold bond the households operating as investors will be able to lend money to the government by investing in a bond whose price is based on the price of fixed amount of gold. After the sales of the gold bond, the bond holder will receive an amount equivalent to the value of gold on that date. This scheme failed because it was faulty. Gold bond buyers do not enjoy the liquidity that a physical gold buyer does. There is a lock-in period for gold bonds of eight years. On the other hand, someone buying physical gold does not have to follow any such restrictions. Though selling in exchanges is allowed, there is no secondary market for gold bonds. Finally, a gold bond buyer exposes himself to scrutiny, while there is still room for anonymity for physical gold buyers. Unless these issues are addressed, the gold bonds are unlikely to pick up.

**3) Indian Gold Coin:** Under the Indian Gold Coin, the government decided to issue gold coins, having Ashok Chakra engraved, at national level. The coins of weight 5 and 10 grams will be issued first, followed by 20 grams. It is estimated that there will be 15,000 gold coins of 5 grams, 20,000 gold coins of 10 grams and 3750 bars of 20 grams. Poor marketing by the government for its gold monetisation scheme (GMS), sovereign gold bond and Indian gold coin scheme is why these have had poor public responses, says the India Gold Policy Centre (IGPC) at the Indian Institute of Management here (IIM-A).

## CONCLUSION AND SUGGESTION

Knowing the fact that India has 20,000 tonnes of idle household gold lying, India cannot be taken up as a poor country. Instead, people should take advantage of this opportunity to bring gold in circulation so that India can reach to its golden period once again.

Poor marketing by the government for its gold monetisation scheme (GMS), sovereign gold bond and Indian gold coin scheme is why these have had poor public responses, says the India Gold Policy Centre (IGPC) at the Indian Institute of Management here (IIM-A).

If the government brings some effective policies, then it is possible that the customers of gold can have the trust to use their gold in the economic growth. There should be long-term measures so that the gold can be circulated in the market. Also, the infrastructure of the gold market has to be upgraded. The standard bars should be raised for the price as well as quality check. Not only the government, but also the banks should keep gold in the terms of liquid reserves. Thus, if the proper policies are followed, gold can turn as a real asset for India. Additionally, it has to be remembered that the government can only put a check on the domestic price as well as imports because the gold price is set in terms of international factors.



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