

Demand for Gold in a Changing Investment Scenario – A Study in Ernakulam District

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 drsanstpeters@gmail.com
 www.commercespectrum.com

Siby Abraham¹

Assistant Professor, P.G. Department of Economics & Research Centre, Sacred Heart College, Thevara, Kerala, India, Email: sibyabrahamc@gmail.com

Abstract

The Household investment pattern of Kerala has been witnessing significant changes in the past two decades. Various avenues of investment are available for a person with surplus fund. Traditionally, the people of Kerala had an affinity towards gold; and their investment in gold has gradually increased over the years. Gold has emerged as the second most preferred investment after bank deposits. Gold, displays an extremely positive feature of low correlation with most of the other asset classes. Investors need to weigh the risk-return ratios of various asset classes carefully to construct a judicious mix of investment portfolio, which meet their specific needs depending on their risk profile, expectations of returns and need for liquidity. The study attempts to assess the changing investment trend in gold with the emergence of various online and offline platforms and products. A sustainable mode of investment is the need of the hour for an industry-starving state like Kerala. . This study attempts to assess the changing investment trend in gold with the emergence of various online and offline platforms and products.

Key words:

Investment, Gold, Assets, Portfolio

Introduction

Gold has been a much sought-after precious metal for coinage, jewellery and other arts since long before the beginning of recorded history. Empires and nations possessed gold as a medium of international exchange, as a store of wealth and as a symbol of power and prestige. The metal outweighs other avenues in universal acceptance and liquidity compared to various other physical and financial assets. It also acts as an effective hedge against economic and political uncertainties.

The global demand for gold arises mainly from four components: jewellery use, industrial use, investment purpose and purchase by the official sector. The largest component of demand is jewellery, which has accounted for 50 percent of the total, followed by investment demand including central bank purchases which has accounted for a further 39 percent. Industry accounts for the remaining 11 percent. While jewellery was typically the largest single component of demand, its share has decreased over the past years in favour of investment demand, as investors have refocused on the wealth creation properties of gold.ⁱ India is the largest consumer of

gold, accounting for over a fifth of annual global gold demand. India depends heavily on gold import, and only a 10 percent of domestic demand being met by domestic supply. This demand remains unabated, despite the increase in gold prices.ⁱⁱ However, the demand for gold in India for Q3 2016 was at 194.8 tonnes, down by 28 percent as compared to overall Q3 demand for 2015 (271.1 tonnes).ⁱⁱⁱ

In Kerala, gold is more a social symbol than a priced investment and it is embedded in the culture. Of the total demand for gold in India, 45 percent comes from Southern States, and Kerala is the leading gold purchasing state among them. The surge in prices has strengthened the gold market in the state and market figures show that there has been no let up in retail buying, as gold is an integral part of marriage, cutting across caste and community divides in Kerala. Traditional loyalty to gold coupled with lack of other investment avenues in the industry-starved state has made gold and land the only investment options⁴. Besides other benefits, consistent demand, world-wide acceptance and supply constraints ensures safety on its valuation.

ⁱ World Gold Council (2011), Gold: Alternative Investment, Foundation Asset, www.gold.org

ⁱⁱ World Gold Council (2012), The Impact of Inflation and Deflation on the Case for Gold, Oxford Economics.

ⁱⁱⁱ Sutanuka Ghosal (2016), <http://economictimes.indiatimes.com>, accessed on 20.02.2017.

¹ **Corresponding author:**

Assistant Professor, P.G. Department of Economics & Research Centre, Sacred Heart College, Thevara, Kerala, India, Email: sibyabrahamc@gmail.com

In the light of changing economic environment, especially when land transactions are subject to high level screening & scrutiny and burgeoning tax rate for land transactions, an understanding of the changing investment pattern of Keralites and its impact on demand of gold as an investment avenue is deemed essential.

Statement of Problem

Buying gold has been an age old practice in Kerala. However, people are generally not aware of its investment potential. The value of gold has increased many folds in the past two decades and has shown more returns than a traditional bank deposit or investments in stocks and mutual funds. An investor has numerous options to choose from, depending on his risk profile and expectation of returns. Different investment options represent different risk-reward trade off. An investor's risk tolerance plays a key role in choosing the most suitable investment. Of the various investment options available in the market, investment in gold happens to be one of the best to be included in the portfolio of an individual. In Kerala, the investment in gold is relatively lower due to low awareness among the investors and the sentimental attachment of them towards holding gold as ornaments. The present study unravels the demand of gold as an investment asset in the changing environment.

Objectives of the Study

The following are the main objectives of the study:

- 1) To evaluate the role of gold in investment portfolio among the households of Ernakulam District, Kerala.
- 2) To examine the demographic profile of households in Ernakulam District, Kerala.
- 3) To analyze the investment trends of households in gold in Ernakulam District, Kerala.

Research Methodology

The study was accomplished by using primary data and secondary data. Primary data was collected by conducting a sample survey among the households in Ernakulam District by administering a structured questionnaire. Convenience method was adopted to collect data from a sample of 250 households. An in-depth review and analysis of secondary information available in the published form was made, which includes data from journals, magazines, reports of research institutes, Government records etc.

Significance of the Study

In India, gold has attained the status of an investment asset only in the new millennium. Investment demand of gold has sparked numerous innovations in gold investment, ranging from online bullion sales to gold Exchange Traded Funds (ETFs). Gold investment avenues have further widened with the introduction of gold certificates, gold accumulation

plans, investment in gold mining stocks and gold futures and options. Recent research has uncovered a number of new practical uses of gold. The potential to use nanoparticles of gold in advanced electronics, glazing coating and cancer treatment offers promising new areas of scientific research. There are good reasons to expect investment demand to remain strong. First, gold has been one of the few assets to deliver on its diversification promise during crisis, in contrast to many other assets. Again, gold has proved to be an asset that protects the value of investment against inflation and dollar depreciation. Past studies reveal, Kerala is one of the largest consumer of gold in the southern states of India, as Keralites especially women holds a sentimental attachment towards holding gold as ornaments. An understanding as to how far the high literacy rate, increasing standard of living index with changing legal environment has brought in a change in investment pattern of households holds significant.

Limitations of the Study

The area of the study is confined to Ernakulam district only, so that it may or may not be relevant and applicable to other parts of the state or nation. The survey was limited to 250 households in Ernakulam district and hence further generalisations could not be made. The responses of the interviewees could be biased and the study being a sample survey reflects all the limitations of such a study. The results of the study could be influenced by such factors which are beyond the control of the investigator.

The Literature Review

According to Ritu and Ankur (2012), the role of gold has increased not only as a store of value but also as an important alternative asset class providing investment benefits. If the returns on bonds, equities and real estate are not adequately compensating for the risk involved and the rate of inflation, then the demand for gold and other alternative investments such as commodities increases. Nigel Desebrock (2002) holds that in India, while cultural, adornment and other factors influence the purchase of gold jewellery, its parallel role as an investment is also relevant and that demand tends to be sensitive to the movements in the price of gold. He opines that the attitude of owning gold jewellery for 'adornment' and 'investment' purposes are no longer homogenous across the population. Among the urban or rural, rich or poor and young or old, they have started to diverge. This divergence is the outcome of varying rates of economic and social change among the different population groups.

The Associated Chamber of Commerce and Industry of India (2012) have examined India's gold import trends since import liberalization during 1999-2000 to 2010-2011. Being the largest importer

of gold in the world, India accounts for nearly one-third of the annual demand with import bill rising from \$4.1 billion in 2001-2002 to \$33.8 billion in 2010-2011. The study noted that India imported more gold than the annual budgeted estimated expenditure outlay on water supply, urban development and sanitation. India's gold demand is 37.6 per cent more than that of China, although China's GDP is 3.5 times that of India. The study also highlighted that gold as a commodity does not add much to the productive capacity of an economy and the foreign exchange reserves used to import gold can be used to purchase other essential commodities. Even as the price is set to move up further, the number of people investing in gold is also on the rise while the benefits of the investment are also growing.

Denver Gold Group (2010), report that gold has served three important functions. It assumes the role of a financial asset, held by individual investors as a store of wealth and has proven as a premium portfolio diversifier. It has been a commodity, used primarily in jewellery but also in electronics, dentistry, and many other technological applications. Finally, it has been a monetary asset, used by governments as a reserve asset, as a form of money, and as a backing for their own currencies.

Roche (2010) observes that, when analysing the price of gold, it is important to understand that gold price do not move like most of the other commodities. It has certain built-in unquantifiable characteristics that drive the price. The price of gold is actually a function of four things: its replacement potential for the U.S dollar, the future rate of inflation, sentiments - generally fear based, and true supply and demand.

Table 1: Gold price in Kerala

Year	Date	Price of 1 pavan gold (Rs.)
1925	31-March-25	13.75
1950	31-March-50	72.75
1975	31-March-75	396
2000	31-March-00	3,212
2001	31-March-01	3,073
2002	31-March-02	3,670
2003	31-March-03	3,857
2004	31-March-04	4,448
2005	31-March-05	4,450
2006	31-March-06	6,255
2007	31-March-07	6,890
2008	31-March-08	8,892
2009	31-March-09	11,077
2010	31-March-10	12,280
2011	31-March-11	15,560
2012	31-March-12	20,880
2013	31-March-13	22,240
2014	31-March-14	21,480
2015	31-March-15	19,760
2016	31-March-16	21,360

Source: Kerala Gold.com

Data Analysis

In Kerala, buying gold ornaments is part of the culture for generations apart from being a favorite gift at marriages and festivals. Higher levels of foreign remittances in the state help the households to maintain a higher saving and prompt them to go for the precious metal. The survey was conducted in Ernakulam District among 250 people of varied income groups.

Table 2: Age Composition

Age Classification	Frequency	Percent
21 - 30 Years	7	2.8
31 - 40 Years	22	8.8
41 - 50 Years	117	46.8
51 - 60 Years	92	36.8
61 - 70 Years	12	4.8
Total	250	100.0

Table 3: Gender Composition of Investors

Gender	Frequency	Percent
Male	212	84.8
Female	38	15.2
Total	250	100.0

Table 4: Educational Qualification

Educational Qualification	Frequency	Percent
SSLC and Below	60	24.0
+2 and ITC etc	48	19.2
Diploma	11	4.4
Degree	75	30.0
Professional Degree	13	5.2
Post Graduation and above	43	17.2
Total	250	100.0

Table 5: Income-wise classification of investors in gold

Annual Income	No. of respondents	Total respondents
₹ 50,000 - ₹ 1,00,000	30	30
₹ 1,00,000 - ₹ 2,00,000	48	78
₹ 2,00,000 - ₹ 4,00,000	69	147
₹ 4,00,000 - ₹ 6,00,000	35	182
₹ 6,00,000 - ₹ 8,00,000	21	203
₹ 8,00,000 - ₹ 10,00,000	16	219
₹ 10,00,000 and above	11	230

Out of the 250 people surveyed, 20 of them had given reasons for not investing in gold. 12 respondents cited lack of surplus fund as the major reason. A few of them believe that gold investment is quite risky and hence refrain from investment. Four others find better value in other assets than gold.

Table 6: Investment assets owned by the respondents

Assets	No. of investors	In percentage (%)
Gold	230	92
Real Estate	160	64
Bonds	25	10
Stocks	95	38
Bank Deposits	215	86
Public Provident Fund	40	16
Life Insurance Corporation	195	78
Mutual Funds	85	34
Others	19	7.6

The table indicates that 92 percent of the sample population has assets in the form of gold which reinforces the fact that, Kerala is a major consumer of gold. Real estate is another preferred investment option. It can also be observed that majority of people prefer to have life insurance and bank deposits which lowers the risks involved. Investment in risky assets like stock and mutual funds are also notable.

Table 7: Various types of gold investments

Type investment in gold	Frequency	Valid Percent
Gold Coin and bars	37	16.09
Gold Jewellery	145	63.04
Gold ETF / e-gold	10	4.35
Gold Coins, bars and Jewellery	31	13.48
Others	7	3.04
Total	230	100.0
Missing	20	
Grand Total	250	

It has been found that out of the 230 respondents who invested in gold, 145 of them have the invested only in the form of jewellery. This is a kind of 'pseudo investment' in the sense that they spend more than the actual value of gold in the form of making charges and similar other expenses which will be lost at the time of resale. Moreover, gold in the form of jewellery would be of 91.6 percent purity which is lower compared to pure gold (99.9% purity) in other investments such as gold bars, gold ETFs and e-gold.

Table 8: Source of information for gold investment

Source of information	No. of respondents	Total respondents
Family and friends	112	112
Market analysis using own knowledge	43	155
Journals, magazines and media	70	225
Consult the investment advisor	4	229
Contact reliable investment firms	1	230

Table 9: Reasons behind investment in gold

Reasons behind investment	Frequency	Percent	Cumulative Percent
Savings	78	33.91	33.91
High return	44	19.13	53.04
Liquidity	29	12.61	65.65
Safety	16	6.96	72.61
Price stability	3	1.30	73.91
Convenience	6	2.61	76.52
Others	5	2.17	78.69
Savings and high returns	11	4.78	83.47
Savings and Liquidity	14	6.10	89.57
Liquidity and safety	24	10.43	100.0
Total	230	100.0	
Missing	20		
Grand Total	250		

The survey has proven that more than one-third of the population considers gold as an effective savings instrument. The demand for gold also stems from its characteristics such as high rate of return, liquidity and safety of investment. Some of the respondents have cited the stability of gold price and the convenience to invest as their priority. There are a few investors who buy gold for want of social prestige and similar other reasons.

Findings and recommendations

The study reiterates the people's preference of Gold as a major investment asset. Investors of Kerala are generally risk-averse and a major portion of their savings is converted into investments in low risk assets like gold, bank deposits, and real estate. It has been found that majority of people prefer to invest in physical gold compared to other investment options such as bars and coins, exchange traded funds (ETFs) and e-gold. Many of them have a sentimental attachment towards holding gold in physical form. As gold ETFs and e-gold are recent investment avenues, some of the investors have a skeptical outlook on the returns of these products. It was also observed that gold continue to be a major saving instrument for lower and middle income households. Individuals with higher income are diversifying their gold portfolio with investments in virtual gold. Various characteristics such as liquidity, safety, price stability and a rate of return above the inflation rate drives up the demand for gold.

There are many investment experts who believe that investment in gold as irrational. However, many a times gold has given better return than that of real estate, stock market and bank deposits. In case of gold investments, what is good for individual investors need not be so for the economy. For example, speculative investment in gold aims at capital appreciation which may not contribute to the productivity or the development process of the economy. Excessive speculation in assets like gold and real estate can impair the entire development process. Hence a sustainable way of gold investment should be promoted without compromising the individual and societal objectives. There is disproportionate growth in jewellery demand in the state and it has an adverse economic impact on the society. One justification for gold ornaments was that it can be used as 'a last resort' in difficult times. However, the burgeoning demand for gold ornaments in Kerala, especially the race for changing the ornaments too often to catch up with fast changing fashion trends, has no such justification at all.

Conclusion

During recession, gold price maintained a positive momentum since more and more investors were parking their surplus fund in gold. Thus, the investment motive seems to be the important driver of the gold market especially during times of market

turmoil. Gold can enhance portfolio performance and complement alternative asset allocations by providing 'true' diversification when it is most needed. Gold helps to manage risk effectively in a portfolio, not only by means of increasing risk-adjusted returns, but also by reducing expected losses incurred under extreme market conditions. There is a strong chance for gold to be considered as an asset class on its own merits and a foundation for a model investment portfolio.

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