Gold and Investor's Perspective in Different Market Conditions

Malik Zainab[1]* and Soni Neha[2]
1. Department of Commerce, SICA College, Indore, INDIA
2. Department of Commerce, Arihant College, Indore, INDIA
*simplyzain@gmail.com

Abstract
The investors are always give preference to invest in Gold as a safe and demanding investment since centuries. Now a new trend has been observed that investors are investing into Gold not for the sake of hoarding the commodity as traditionally been observed, but also as the part of the risk mitigation strategy in their investment portfolio. Research shows an analytical perspective from the investor's point of view.

This research shows the data published by reputed journals and institutions on the various inflationary market conditions such as Baseline Inflation, Deflation, Stagflation and High Inflation. That will help readers to understand how the financial markets in emerging as well as developed economies of the world react in order to sustain the economic losses due to these conditions is well explained in this study. At the same time, the analytics show the impact on the Gold within the various inflationary conditions.

Keywords: Gold Investment, India, Market risk, Investment Portfolio, Risk Mitigation, Intrinsic Value.

Introduction

India is a vibrant country with different cultures and sub-cultures, customs, religions, food and ethnic dress preferences. Indians are affectionate for Gold as a part of culture and tradition and keep on accumulating it for many centuries. It is the only commodity which is universal across the length and breadth of the country. It is observed[2] that every class of the Indian society, whether urban or rural investor, would prefer to possess it or make savings to purchase it in their life span. There are myths and strong beliefs that possession of Gold is the sign of prosperity and brings good luck in their lives.

One of the study by Pattanaik observed the main reasons for Indian community being so much passionate about the Gold. He defined it in terms of 'Logical' and 'Cultural'. In logical terms, as he explained in his research study, gold being a tangible asset is also a portable investment. In addition, it is also a beautiful ornament, which could be worn on daily basis. This investment is not just like the shares, bonds or real estate. And secondly gold also has cultural significance, every Indian strongly believes that Gold is very auspicious, divine as well as a sacred metal, whereas Hindu community also considers it as a symbol of their goddess called 'Lakshmi' and worshiping it in this sacred form would bring them with lots of good luck and prosperity in their life. The consumer purchasing trends for the Gold as an investment commodity and its demand in India are expected to grow at the level of 30% in real terms during the next decade.

This rise of demand is backed by the GDP, rapid urbanization, growing strong middle class population as well as rising savings rate of 30-40% of income (as expected to continue for coming decade). This study gives a wider overview of the customer demand for gold as a sound investment in different market conditions. Initially, the study focuses on the reasons for the surge in the demand of Gold among the Indian investor's and then it progresses with explaining the influence of financial markets of the emerging as well as developed economies on Gold and its movements. This report is highly descriptive and analytical based on different market conditions.

Economic and Growth reasons pushing the demands for Gold in India: Current scenario is that since employment opportunities have increased, people started to invest more of their savings into safe, reliable and secure assets which can be used immediately in any needful situation. Due to exponential growth and rise in the income of the Indian consumer, gold has emerged as one of the most preferred investment asset class in India and thus has seen manifold spur in its demand.

Suresh[1] has identified into her recent research study, the demand for gold has been raised as a sustainable investment for any inflationary situations which the country is facing currently. According to the statistics provided by various government agencies, Indian demand is likely to be around 650 tonnes in 2017, compared to a 10-year average of 845 tonnes. The studies conducted reveal the reason for such a high level of demand and investment urge amongst the Indian customers are due to rise in their savings and real income levels, and not by price of the commodity.

In fact, the commodity price value has appreciated many times in the last decade in continuation to the trends in the international markets. It is believed that this GDP and economic development in India would accelerate the level of consumption and thus the demand of Gold in India in coming years.

Change in Investment Outlook: Consumers are always in search for an asset which would maximize their returns and at the same time provide stable growth and returns in the times of economic turmoil. Recently, as India moves on for rapid expansion of economic development, the Indian consumers have started investing more and more of their savings into Gold which has a high level of risk diversifying quality.

The report of Green shows the risk diversifying quality of Gold extensively. In fact, he had empirically also proved that the returns on Gold as investment are independent in comparison with other class of assets. In his study of four hypothetical portfolios of varying risk, he showed the increased level of average return in Gold. Based on his findings and reports published by World Gold Council (WGC*),[2] it could be well suggested that if an investor wishes to invest in an asset, which is largely unrelated to the fluctuations and speculations in the different market conditions, then gold is the best commodity for this purpose. Even, the mutual funds considered for risk mitigation will not be able to give reasonable amount of returns in comparison to Gold.

A new research has been done by WGC (2018) to determine the factors which influence the demand of gold in India. They found that the demand of gold in India was mainly driven by rapid GDP growth, urbanization and the migration of people from rural to urban area within the country as well as rise of income and savings among the people due to economic prosperity. This demand is rapidly increasing at the rate of 3% annually.

These all reflect the notion that Indian investor's are changing their mentality and are no more traditional buyers of commodity such as gold, rather, they see it in terms of safety of their investments in the turbulence period of in the Indian economy which is experiencing the era of stagflation. As documented by Suresh,[1] the Indian investor's are seen, purchasing gold as hedge or safety against economy, political or social crisis and most importantly currency crisis which are resembled by sudden market crashes, currency failures, nation debts, inflation, war and other social unrest.

The studies conducted on the demand of gold in India also revealed the fact that, the demand and value of gold have increased on an average of 13 percent per year, which has super sided the country's real GDP, inflation and population growth, taken altogether by six, eight and twelve percent respectively. The analysis of Indian commodity shows that Indians are saving 30% of their income, out of which 10% is invested only in Gold. They see Gold as a safe and most reliable investment asset class which has helped in surging the prices of this commodity in recent times.

In recent times, looking to the acceleration in the investment demand for gold in domestic markets in India, the government and private investment firms have launched various schemes and products such as Gold Trust and Gold Exchange Traded Funds (ETFs). In comparison to investing money into bonds and stocks which are the forms of equity investments, the consumer's perception towards gold is more definite.

Alternative Economic Market Conditions and Performance of Gold: The analysis has been carried out to compare the performance of Gold with other asset classes such as stocks, bonds, cash and housing prices. The basis of our analysis is the secondary data in terms of a recent report published by the World Gold Council (WGC), as part of the analysis, various market conditions such as Baseline Inflation, Deflation, Stagflation, and Inflation in the market economy which impact the consumer investment decision have been analyzed and compared. The market reactions in terms of various asset classes and their performance have been observed as part of this research study.

Baseline Inflation scenario and Performance of Gold: Baseline inflation scenario is defined as a condition where there is steady economic recovery, inflation level is moderate and the financial conditions are normalized. The study finds that the global recovery is reviewed mostly by the growth taking place in the emerging market countries. The study estimates that the growth rate for the recovery with the emerging Asian countries is expected to be 7-8 % per annum to 2019 while world overall growth rate is about 4 % per annum.

The report finds that during the baseline inflation scenario, US dollar strengthens this and also leads to slightly down ward pull in the prices of gold. The report concluded on the fact that as result of these various factors (negative real rates, wide credit spreads and the rapid expansion of the monetary base), the price moments in gold witness downward trends and underperformed in comparison to other classes of assets from 2011-2015, with the best performing asset class being equities and cash reserves.

Deflation scenario and Performance of Gold: Deflation scenario is defined by a condition, wherein, there is a massive financial shock leading to feeling of recession and fall in the consumer prices. The study finds that the major defaults in the countries associated with Euro zone, are facing major losses. They resort to squeezing their profitably, leading to the fall in the asset prices. Although the inflation in centered in the euro zone, but impacts of the financial crisis are felt globally due to intern linkages with world economies. The government tries to loosen up the monetary policies, impacting the strengthening of US dollar and a positive shift in the real interest rates; it results into the reduction in the credibility of the government. This is a negative effect of deflation. At the same time, the result of comparison of Gold's performance and other assets such as property and share prices, shows that they perform poorly whereas cash and bonds post modest but positive returns.

Stagflation scenario and Performance of Gold: Stagflation scenario is defined by a condition, wherein, there is a high level of inflation and interest rate but at the same time weaker growth in comparison to the baseline inflation. In this condition, the study examines the consequences of the sudden increase in the oil prices to US $ 150 per barrel which was the level in 2008.[2] Because of the sudden hike in the oil prices in the international markets, it transforms into the headline inflation, while triggering the wage inflation amongst the worker community. This results into workers restoring to the savings and investments for maintaining their purchasing power in the economy.

The study finds that due to abrupt slowing down of the world economy in 2012-13; it leads to the loss of investor confidence and rise in the financial stress in the economy, resulting into rise of bad debts and loans. Ultimately, the credibility of Banks have been damaged and they are forced to adopt policies relating to tightening of the credit standards. Despite the conditions created due to stagflation, the study concludes that the gold's relative performance from 2011-15 was better in this scenario in comparison to the baseline inflation while it is lagging that in the deflation scenario.

High Inflation scenario and Performance of Gold: High Inflation scenario is defined by a condition, wherein, there is a double digit inflation which is the resultant factor of the wage-price imbalance and the tight monetary policy. This scenario ultimately leads to the sharp monetary tightening and then into the recession. In this condition, the study finds that during this period, the economic growth at the beginning of the scenario is very strong in comparison to the baseline inflation. This is because of the policy initiatives and the consumer and business confidence which is recovering rapidly, resulting into the narrowing of the margins of spare capacity in the global economy, thus, giving rise to the inflation.

In this scenario, the study finds that due to the high inflation, it has a positive impact on gold. The study finds that during high inflation in US with weaker dollar and negative interest rate, the performance of Gold has been boosted. Further the study observes that as the global economy shifts towards recession later in this scenario, gold also receives a big push due to the rise in the financial stress. This rise is comparable in scale to the recent global and financial crisis as being witnessed.

Conclusion

As observed in part of the study, the investors find Gold as stable investment during different market conditions and can get benefits out of it. Gold's optimal share as part of sound investment in the portfolio rises in a more inflationary case in order to mitigate the risk and ill effects of the returns on the investment into alternative assets. These findings further reveal that the optimal allocation of the investor's fund to different asset classes varies differently based on the perceived risk and change in their tolerance limit based on the economic and market conditions.

The study finds that investor's with higher risk tolerance are more inclined to allocate and invest into riskier assets such as equities, whereas the low risk investors allocate and invest more into so called 'safe' assets such as cash and bonds. India is fast developing country in economic sector and the investment and demand into commodity such as Gold has been recently on rise in India. In future it would be interesting to further investigate the impacts of gold on inflation rate in the Indian Economy. More empirical research would be required wherein a new framework could be derived using Gold as a mechanism to keep down the level of inflation rate to the baseline inflation.

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