

GOLD PRICES AND INDIAN SPOT FX MARKET

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ABSTRACT

In India gold is a vital part of household savings for a large number of investors. Even for the financial markets, Gold has been a valuable investment option, an alternative to the U.S dollar, and even as a hedge against inflation. Thru the recent years there has been a sustainable rise in the international gold price, also effecting gold price in India. This paper has made an attempt to spot out what are the possible impacts of Gold price fluctuation in Indian Spot FX Market.

Paper has tried to cover connection between the Gold price and Indian FX Spot Market.

Reserve Bank of India denotes Gold as a currency, the only difference is this currency can only be traded against USD, and its currency code is XAU which is accepted international.

INTRODUCTION

Precious metals like Gold, Silver, Platinum and Palladium, have some inherited value attached to it. It is because it has the capability to store a good sum of amount in a rather small piece. Gold has been widely used throughout the world as a vehicle for monetary exchange. As a result, Gold has always been a valuable investment option not only for households but also for the big investors and also people stock gold to protect them self from inflation. In last few year price of gold have risen drastically the acceleration in gold price was much faster than any other asset class. And in spite of such sharp upward trend we have seen an increase in demand of gold in India. Gold investment is done in the same way as with foreign currencies. Gold trading is directly between the seller and the buyer. The demand of gold in India has only gone up despite of increase in gold price. All this demand by Indian buyer is met by gold importer in the country; one of the biggest imports of gold in India is done by MMTC (Mineral and Metal Trading Corporation). In recent times gold among the major assets classes has given maximum return on investment. A process of shifting gold from regulated to deregulated market was started in 1991. The shift for this was first highlight in Committee on Capital Account Convertibility (CCAC). This committee also recommended removing import duty on gold to reduce smuggling. It is said that the Domestic gold price should almost move in same magnitude as international gold price, and also with rupee's appreciation and depreciation it should

increase or decrease. However in really scenario its is not true that rupee moves only on bases of gold price movement. Recently as per the new financial policy government have revived the import duty on gold.

Impact of Gold price on FX Spot Market in India

Gold has been widely used throughout the world as a vehicle for monetary exchange. Precious metals like Gold, Silver, Platinum and Palladium, have some inherited value attached. Gold have strong ties with USD movement. Gold is mostly traded against USD across the globe, and unlike in Kilos how it's traded in India, in international market it is traded in ounces. There is defiantly an inter-relationship between International Gold price and Domestic Price which is clear from the graph below. (Where red line indicate international gold price and blue line indicates gold price against INR)



Source: Thomson Reuters

However Gold is considered as a currency in the international market, and is traded even in Over the Counter across the globe, it is denoted by XAU. It is said that with domestic gold price increase/decrease, Rupee should also depreciation/appreciation. In the really scenario apart from USD being common for both INR and XAU, there is nothing else which drives the price for both the currency. So ideal when the price of the gold goes up per ounces, the rupee value should weaken against USD. In below graph (the red line shows the price of gold and blue line shows rupee)

