Investing in Gold Bonds

Why in news?

Fourth tranche of sovereign gold bonds 2020-21 are opened for subscription.

What are gold bonds?

- The government introduced the gold bonds scheme in 2015.
- The scheme was introduced to wean away investors from the physical gold market.
- These bonds have a maturity period of eight years.
- But, the investors have the option to exit after the fifth year.
- Funds raised through such issuances form part of the government's overall borrowings in a year.

What are the benefits of buying gold bonds?

- Gold bonds offer investors twin benefits of price appreciation along with a fixed 2.5% coupon per year.
- Interest earned on these gold bonds is added to the holders' income.
- Interest earned on these bonds is taxed according to their slab rate.
- Any capital gains on these bonds at maturity are tax free.
- This makes them far more attractive than owning physical gold.
- To offer greater liquidity, the bonds are listed on stock exchanges within a fortnight of issuance, and can be traded.
- Gold bonds appear attractive when gold prices spike.
- This leads to greater investor interest in this asset class.

Why are gold prices rising globally?

- Much before Covid-19's impact led to a crash in global stock markets, gold prices had started their upward glide.
- The global **spread of Covid-19** has raised concerns on global growth over the last three or four months.
- **Negative growth rates** and **fears of a global recession** have

- pushed central banks and big investors to take shelter in gold.
- There is nearly 40% crash in benchmark equity indices in the US between February and March 2020.
- This has forced the US Federal Reserve to announce a record liquidity injection and bond-buying programme of more than $3 trillion.

Why prices are rising in India?

- Since **India mostly imports gold**, the depreciation of rupee with regard to dollar makes gold costlier in India.
- **Domestic factors** such as concerns over the country's fiscal health and a higher demand for gold also pushes up prices.
- In India, the RBI has cut policy rates by 115 basis points over the last three months, and brought down the repo rate to 4%.
- [Repo rate - The rate at which the RBI lends to commercial banks]
- The RBI has also announced liquidity injection in the economy.
- Any expansion in the paper currency tends to push up gold prices.

Will gold prices continue to rise?

- Gold is an efficient tool to hedge against inflation and economic uncertainties.
- It is also more liquid when compared with real estate and many debt instruments.
- Generally, after any major economic crash and recession, gold prices continue their upward run.
- Market analysts feel that gold could overtake its previous peak of around $1,900 per ounce in the global market.

Can one invest in gold at the current price point?

- In India, there is a sharp decline in interest rates over the last year alongside high volatility in the equity markets.
- This has brought investors' focus towards gold.
- A cut in interest rates by the RBI has led to a decline in interest rates on small savings and term deposit rates of banks.
- SBI is currently offering an interest of 2.7% on savings bank deposits, and 5.4% on 5-10 year term deposits.

- Experts say that it makes good sense for investors to invest in gold.

Can the price of gold crash?

- Given the economic uncertainty, gold would touch a new all-time high.
- In India, prices will be supported by any further weakness in rupee.
- Key events that could stall the rise of gold are,
    1. Sudden sale of gold holdings by central banks to tide over the economic crisis,
    2. Crisis in other risk assets prompting investors to compensate their losses through sale of gold ETFs (Exchange Traded funds).

Source: The Indian Express