

RBI's Surge in Gold Reserves

Why in news?

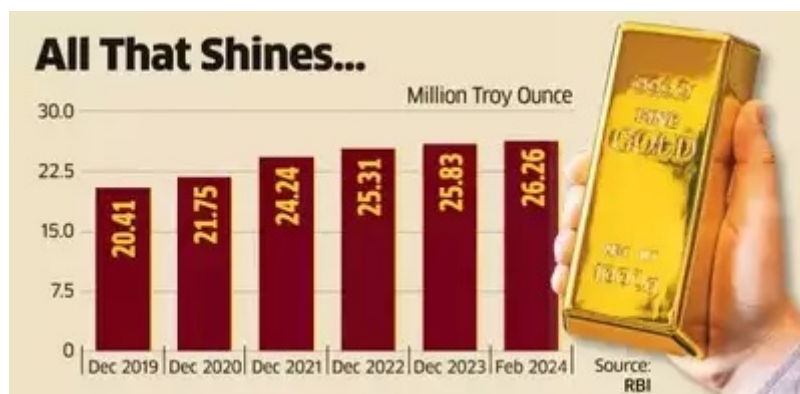
RBI has increased gold purchases to diversify reserves, with gold value contributing to a 3 billion dollars rise in forex reserves to 648.5 billion dollars.

What is the status of RBI's gold reserves?

- The Reserve Bank of India has increased its gold purchases, significantly boosting its foreign exchange reserves with 3 billion dollar rise reaching a record 648.5 billion dollars.
- The RBI has bought approximately 13.3 tonnes of gold (between January-February 2024), accounting over *80% of its total purchases* in 2023.
- RBI has *consistently buying gold* since 2017 to diversify its foreign currency assets and hedge against inflation and forex risks.
- The proportion of gold in India's total foreign exchange reserves has increased from around 7.9% in early April 2023 to approximately 8.41% in early April 2024. But it's important to note that the central bank holds only a portion of these reserves domestically.
- A significant portion is held abroad, with custody arrangements in institutions such as the Bank of England and the Bank of International Settlements (BIS).

Why RBI is buying gold?

- **Safe haven asset**- Gold is traditionally viewed as a safe haven asset during times of economic and political instability, gold's intrinsic value and status as a globally recognized store of wealth contribute to its appeal as a reserve asset.
- **Russia-Ukraine conflict**- Heightened uncertainty in the global geopolitical landscape has diminished US dollar as stable currency, this underscores the importance of diversification and risk management in reserve management strategies.



- **Surge in gold price**- The surge in international gold prices has bolstered the value of

the Reserve Bank of India's (RBI) gold reserves as this increase in value reflects both the quantity of gold held by the RBI and the prevailing market price of gold.

The RBI's gold reserves are typically valued based on prices quoted on the London Bullion Market Association (LBMA), one of the world's leading precious metals markets.

- **Volatility in Forex market**- Gold historically has served economic uncertainty, geopolitical tension etc., compared to currencies hence gold is perceived as more stable stores of value.
- **Raising interest rate in US**- When interest rate rise in the United States, it can affect global financial market as they reduce liquidity in emerging markets and increase borrowing costs. Hence central banks diversify their reserve assets, including their holding of gold to hedge against potential adverse effects of rising US interest rates.
- **Diversify asset classes**- Gold offers diversification benefits because its price movements often behave differently from those of other asset classes, such as equities or bonds.

RBI aims to diversify its reserves with gold accounting for about 8.41% of total foreign exchange reserves in value as of early April 2024.

- **Global economic shifts**- The move reflects a broader trend of declining confidence in dollar assets among central banks, with a noticeable drop in US treasury bond holdings from 50.1% to 47.2%.
- **Weakened dollar**- Currently, US bonds are at their highest yields, indicating a weakened dollar compared to its past strength, despite being the dominant currency in global trade.

Foreign Exchange Reserve

- **About**- Forex reserves are assets maintained by *monetary authorities* to check the balance of payments, deal with the foreign exchange rate of currency and to maintain financial market stability.
- **Governed by**- RBI Act, 1934 and the Foreign Exchange Management Act, 1999.
- **Composition**- India's forex reserves can be broken into four categories.
 - Foreign currency assets
 - Gold
 - Special drawing rights
 - IMF's Reserve Tranche Position

Why gold is an important component in foreign exchange reserve?

- **Commodity-linked currencies** - Gold has performed even better when expressed in terms of commodity-linked currencies.
- **Increasing value of gold** - The rate of the gold has been increasing more than the US dollar.

- **Weak global financial system** - The financial system is expected to face several crisis because of more volatility.
- **Foundation for the rupee** - Gold reserves coupled with a strong economy, balanced current account deficit and good balance of payment lay the foundation for the rupee in long term.

What lies ahead?

- RBI by maintaining a diversified reserve portfolio that includes gold alongside other assets, aims to enhance the stability and resilience of their reserves, ultimately supporting their broader monetary and financial stability objectives.
- RBI can reduce exposure to any single asset class or currency due to diversified reserves, this strategy helps safeguard reserves against volatility, economic shocks, and geopolitical uncertainties.

Quick facts

Bank of International Settlements (BIS)

- **Established year**- 1930.
- **Ownership**- It is owned by 63 central banks including RBI that account for 95% of the GDP.
- **Head office**- Basel, Switzerland.
- **Representative offices**- Hong Kong and Mexico City.
- **Mission**- To support central banks pursuit of monetary and financial stability through international cooperation and to act as bank for central banks.
- **Basel Committee on Banking Supervision**- It provides the Basel norms.

References

1. [Times of India- Why RBI is buying gold?](#)
2. [BIS- About BIS](#)