Sovereign Gold Bond - A Financial Innovation in India

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Abstract
Sovereign Gold Bond is one of the major initiative that was taken by the NDA government in the year 2015. As per the definition given by Reserve Bank of India, SGB are the securities denominated in grams of gold and are the substitute of physical gold. These bonds come under the purview of Reserve Bank of India and are more safer. The present paper will explain the theoretical framework and background of Sovereign Gold Bond and its comparison with that of Gold ETF and physical gold. The paper will also try to find out the yield analysis of SGB. The present paper will shed a light on the steps which can lead to proper implementation of Sovereign gold Bond Scheme in India.

Keywords: *Sovereign Gold Bond Scheme, Gold, Yield and Gold ETF*

I. INTRODUCTION

Gold is considered to be an auspicious and precious metal among the Indians. However, the making charges of gold serves as a constraint in the gold affordability. As a result, Government of India and Reserve Bank of India have come up with various alternatives like gold ETF, Sovereign gold bond scheme, etc. In other words, now one can own gold in certificate format. Sovereign gold Bond is one of the prominent schemes of government which offers an investor a best way to own gold. The scheme came into the limelight in the Union Budget 2015-16. The scheme was formally launched by the Prime Minister of India Shri Narendra Modi on 5 November 2015. From June 2016 onwards SGB started trading on the National Stock Exchange (NSE) and Bombay Stock Exchange(BSE). SGB intends to target that investor who wants to purchase gold for investment purpose. As per KUB Rao Committee report in 2013, it was mentioned that more import of gold is putting strain on the stability of India's external sector. Inability to meet more demand of gold led to larger gold import which in turn puts strain the India's current Account Balance. Thus there was a need to introduce scheme like SGB so as to reduce physical demand of gold. Earlier Gold schemes in India were based upon the acceptance of gold deposit and issuance of gold bond in return. But in SGB scheme, gold bond are issued in return of payment of rupee. SGB has been emerging as a best substitute of physical gold.

II. LITERATURE REVIEW

(Adhana, 2015) in her paper explained the probable impact of sovereign gold bond scheme on current account deficit. The paper also highlighted certain steps for the successful implementation of gold schemes. Better policy implementation, stabilising gold market, infrastructure and human resource development, etc are some of the steps which helps in accelerating the growth of SGB scheme.(Erb, 2014)_explained that the demand for gold and bonds depends upon the market fear. If market fear diminishes, the impact on gold's prices could be significant.(Singh, et al., 2015) in their paper explained the governance and regulation of gold market in India. More and more import of gold has lead to increase in Current Account Deficit(CAD). Thus policy measure need to be taken so as to make gold policy independent of CAD.(Rathore, 2017) in his paer highlighted the attitude of investor towards physical god and Sovereign Gold Bond Schemes.The paper shed a light on the signifcance of demographic factors.These factors do have an impact while taking gold investment decisions. Investor awreness for SGB schemes is still very moderate. Thus investment in SGB is not at par with that of physical gold investment.The similar reults were highlighted by (Arora, 2016) in his paper. Ammendment in various provisions of SGB like reducing minimum investment size are some of the initiative which can make this scheme more attractive among the investors.(Muharam, 2013) in his paer explaines the factors influencing government bond yield wherein inflation and real sector performance have no impact on government bond yield.

III. OBJECTIVES

- ➢ To study the conceptual framework and theoretical background of Sovereign Gold Bond scheme.
- ➢ To understand the difference between SGB, physical gold and Gold ETFs
- ➢ To find out the yield of SGB bond of Different series.
- ➢ To explore various steps that can lead to proper implementation of SGB scheme.

IV. RESEARCH METHODOLOGY

The research paper is based upon the secondary data analysis. Various books, journals, articles have been analyzed to study the past, present and future prospects of SGB scheme in India. Data have also been collected from Reserve Bank of India site and analysis has been done using MS excel.

V. THEORETICAL BACKGROUND

SGB comes under debt fund category. These are the transparent instrument as they come under the purview of RBI. Making investment in such funds save investor's money as he don't need to make payment for making charges. SGB are government securities and hence they are safer. One need not to hire a bank locker for it. If a person wants to purchase a bond them he can simply approach to SEBI authorized agent and can enjoy benefit associated with SGB scheme. At the time of redemption, the amount will get deposit in your registered bank account. SGB are the low risk investment and are the perfect for more risk averse investors. The bonds also fetch a fixed interest income to investors. Nominal buying and selling of SGB is one of the important benefit derive from these bonds. SGB are kept in demat form, thus no one can steal it because they are in paper form. These are the long term investment avenues which provide good return to bondholder. Any person who is a resident of India can purchase these bonds for investment purpose. One can also invest on behalf of minor. The minimum and maximum investment limit in SGB is 1gm and 4kg of gold per investor (individual and HUF) while the maximum limit for entities is 20kg. SGB bears a fixed maturity period of 8 years with a facility to exit from such scheme after 5 years. Both cash and digital payments are allowed to purchase these bonds. These bonds bear a fixed interest of 2.5% annually and returns are linked to gold's market price. If investor decides to transfer the bond then he can receive indexation benefits along with long term capital gain. SGB redemption are exempted from tax deducted at source. They can be counted towards Statutory Liquidity Ratio if bank have acquired the bonds after going through the process of raising lien. The redemption price of SGB is based upon the average price(last three working days) of gold. The trading of these bonds occurs either through recognized stock exchange or through intermediaries.

VI. BENEFITS OF SGB

- They are much safer financial instrument as there is no risk of theft which is generally there in case of physical gold. They are in paper form and no one can steal it or change its ownership.
- Being a bond category, they provide a fixed interest income of 2.5% to investors.
- These bonds provide indexation benefit to investor if he chooses to transfer the bond before the maturity.
- Investor can easily sell these bonds after the lock in period of 5 year on NSE or BSE. Thus they are liquid as well as marketable also.
- SGB are often accepted as collateral by some banks against secured loan.

VII. COMPARING SGB WITH PHYSICAL GOLD AND GOLD ETF

Return generated from Sovereign Gold Bond are higher than that of actual gold which is exactly opposite in case of gold ETF. Return on physical gold also gets reduces because of the making charges associated with it. As stated earlier, SGB are the safer financial instrument as compared to physical gold. SGB and Gold ETF are in electronic form hence they are more pure but the purity of gold always remains a question in case of physical gold. Gold ETF can't be accepted as a collateral while SGB and physical are generally accepted as a collateral. Gold ETF and SGB are tradable but there are restrictions on the tradability of physical gold. Storage expenditure is minimum in case of SGB and Gold ETF. In other words, Sovereign Gold Bonds are superior in almost every aspect as compared to gold ETF and physical gold.

VIII. FINDINGS

S No	Series	Settlement Date	Maturity (5Yrs)	Maturity(8yrs)	Maturity(10 yrs)	Coupon Rate	Issue price/ unit	Redemption	Frequency	Basis	Yield(5 yrs)	Yield(8 yrs)	Yield(10 yrs)
1	2015-I	26-Nov-15	26-Nov-20	26-Nov-23	26-Nov-25	2.75	2684	2835	2	0	0.11	0.11	0.11
2	2016-I	08-Feb-16	08-Feb-21	08-Feb-24	08-Feb-26	2.75	2600	2798	2	0	0.12	0.11	0.11
3	2016-II	29-Mar-16	29-Mar-21	29-Mar-24	29-Mar-26	2.75	2916	2780	2	0	0.09	0.09	0.09
4	2016-17 Series I	05-Aug-16	05-Aug-21	05-Aug-24	05-Aug-26	2.75	3119	2800	2	0	0.07	0.08	0.08
5	2016-17 Series II	23-Sep-16	23-Sep-21	23-Sep-24	23-Sep-26	2.75	3150	2800	2	0	0.07	0.08	0.08
6	2016-17 Series III	17-Nov-16	17-Nov-21	17-Nov-24	17-Nov-26	2.75	2957	2783	2	0	0.08	0.09	0.09
7	2016-17 Series IV	17-Mar-17	17-Mar-22	17-Mar-25	17-Mar-27	2.75	2893	2813	2	0	0.09	0.09	0.09
8	2017-18 Series I	12-May-17	12-May-22	12-May-25	12-May-27	2.75	2901	2791	2	0	0.09	0.09	0.09
9	2017-18 Series II	28-Jul-17	28-Jul-22	28-Jul-25	28-Jul-27	2.75	2780	2770	2	0	0.10	0.10	0.10
10	2017-18 Series III	16-Oct-17	16-Oct-22	16-Oct-25	16-Oct-27	2.75	2956	2798	2	0	0.08	0.09	0.09
11	2017-18 Series IV	23-Oct-17	23-Oct-22	23-Oct-25	23-Oct-27	2.75	2987	2880	2	0	0.09	0.09	0.09
12	2017-18 Series V	30-Oct-17	30-Oct-22	30-Oct-25	30-Oct-27	2.75	2971	2845	2	0	0.09	0.09	0.09
13	2017-18 Series VI	06-Nov-17	06-Nov-22	06-Nov-25	06-Nov-27	2.75	2945	2800	2	0	0.09	0.09	0.09
14	2017-18 Series VII	13-Nov-17	13-Nov-22	13-Nov-25	13-Nov-27	2.5	2934	2750	2	0	0.07	0.08	0.08
15	2017-18 Series VIII	20-Nov-17	20-Nov-22	20-Nov-25	20-Nov-27	2.5	2961	2791	2	0	0.07	0.08	0.08
16	2017-18 Series IX	27-Nov-17	27-Nov-22	27-Nov-25	27-Nov-27	2.5	2964	2751	2	0	0.07	0.08	0.08
17	2017-18 Series X	04-Dec-17	04-Dec-22	04-Dec-25	04-Dec-27	2.5	2961	2790	2	0	0.07	0.08	0.08
18	2017-18 Series XI	11-Dec-17	11-Dec-22	11-Dec-25	11-Dec-27	2.5	2952	2810	2	0	0.08	0.08	0.08
19	2017-18 Series XII	18-Dec-17	18-Dec-22	18-Dec-25	18-Dec-27	2.5	2890	2820	2	0	0.08	0.08	0.08
20	2017-18 Series XIII	26-Dec-17	26-Dec-22	26-Dec-25	26-Dec-27	2.5	2866	2791	2	0	0.08	0.08	0.09
21	2017-18 Series XIV	01-Jan-18	01-Jan-23	01-Jan-26	01-Jan-28	2.5	2881	2787	2	0	0.08	0.08	0.08

IX. RESULTS

- Inverse relationship between SGB and yield. Decrease in bond price from Rs 2684 to Rs 2600 increases the yield from 11% to 12%[2015 -1 & 2016-1]
- Yield of 5yr bond is slightly lower than that of 10 yr SGB
- Approx. yield of SGB lies between 8-12%

X. CONCLUSION

The awareness of Sovereign Gold Bond scheme among the investors is still very moderate. Many investors still believes physical gold as a safer option irrespective of interest government may provide. There is still lack of income tax clarity on few provisions of SGB. There is a need to stabilize the gold market. The government must take adequate measures to reduce the demand for gold by making necessary changes in the gold policy. The government must ensure proper standards and regulation so as to improve the governance issue in the market. There is a market risk associated with SGB. If prices of gold falls then it will leads to capital loss on investment. Moreover, there SGB are illiquid in the first 5 years. Taxability of interest earning and non compounding of interest are another major concern which distracts the investors to invest in this scheme. Appropriate measure needs to be taken to improve the marketability and tradability of SGB. Government has also taken some initiative so as to popularize this scheme. In order to meet the investment needs of different category of investors, flexibility has been given to introduce various variant of SGB with different interest and risk protection payoff. Despite of these concerns, SGB have a vibrant market in the near future. Such type of scheme is necessary to improve the overall health of economy.

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