

# Riding on global moves

Despite contraction in demand gold prices have surged to a record high. Will it sustain?



**A**head of the festive season starting mid-September, gold prices in India created a record of sorts by cresting the ₹31,000 per 10 gm mark last fortnight. The strength in the rally saw prices rising to ₹31,400 in the subsequent session, before finally settling around ₹30,900 on 29 August. Over the last one month gold gave returns of a little under 4 per cent and more than 9 per cent over the past six months.

While domestic prices are closely linked to global prices the gains in rupee terms is at a variance over dollar gains over the six month period. On 1 March for instance, the dollar price was \$1,718.70 per ounce, higher than the current prevailing price of \$1,656.34 as on 29 August. One of the reasons for the variance is the rupee depreciating against the dollar. The rupee depreciated by 13.25 per cent from 1 March, falling from ₹49.15 to the current ₹55.66.

The factors behind the global rally are well known: expectations of further quantitative easing in the US and eurozone, mounting geo-political tensions in African countries and uncertainties in global markets. Added to these is the higher purchases

of gold by central banks around the globe, which in a way has partially offset the lower consumption in India. According to a report by the World Gold Council (WGC), gold reserves increased by 157.5 tonnes in the second quarter of 2012 as central banks preferred to retain a portion of their reserves in physical assets. The magnitude of this purchase is believed to be the largest since central banks became net purchasers since the second quarter of 2009, following the US subprime crisis. Central banks of Russia and Kazakhstan were among the active buyers.

## Low demand

India and China collectively account for as much as 45 per cent of gold consumption. However, Indian imports which account for nearly 90 per cent of domestic consumption (the balance is recycled gold) has been falling over the last couple of years. In 2011 India imported 933 tonnes, lower as against the 1,006.3 tonnes imported in 2010. In the first two quarters

imports have gone down even further following the government's move to disincentive purchases by raising import duties. The WGC has estimated that overall imports by India will dip to 750 tonnes in 2012. The first six months have already witnessed a demand contraction of 26 per cent. Rising inflation, a depreciating rupee and economic slowdown further contributed to a slow down in the purchases of gold by consumers at higher levels. China may emerge as the biggest buyer in 2012.

Consumers' continuing resistance to the higher price may not see any significant spurt in demand even during the festive season and most analysts expect the prices to remain at higher levels. "Everyone is waiting for a price correction in India. If the rupee appreciates and ECB tightens the monetary policy instead of easing as everyone expects, prices in global markets could see a correction," says Prithviraj Kothari, president, Mumbai Bullion

Association. Kothari says that while economic uncertainties weigh on investors, much would also depend on how the US handles the situation. "Gold could see a high of ₹32,000 on the higher side and between ₹29,700-30,000 on the lower side in the foreseeable future." Kothari also does not expect consumption in India to pick up, significantly.

Besides lower imports, Indians could instead be pressing sales. In which case more gold for re-cycling could limit imports even further. And in the face of falling demand could lead to a sharper correction. India has the highest stock of physical gold, estimated at 14,-15,000 tonnes. Even a 5 per cent sale could well impact prices, even on the global front.

Strong consumer resistance in India could also counter the aggressive buying by China and possibly central banks that have been on a buying spree.

By mid-September one could probably have a better idea on the future price movement of gold.



Kothari: expecting correction