NOTES

IMPORT OF GOLD BY NON-RESIDENT INDIANS

During the three fiscal years 1992-93 to 1994-95 a total of about 428 tonnes of gold, according to official reports, was imported by eligible Non-resident Indians. It is estimated that another 220 tonnes was similarly imported in 1995-96, a total for the four fiscal years of about 648 tonnes. Between April, 1992 and December, 1996, eligible NRI's (i.e. with an absence abroad of six months or more) were entitled to import up to 5 kg gold each on payment of Rs. 22/- per gram import duty. This level of duty, during the above period, averaged about 5% of the U. S. dollar price. From the beginning of the calendar year 1997 the import entitlement per eligible NRI has been increased to 10 kg.

Assuming all NRI imports of gold up to the end of 1996 to have been at the maximum of 5 kg per NRI, the 648 tonnes represents a minimum of 129,600 eligible NRI's returning to India with such gold, or acquiring it after arrival from official sources by paying for it in foreign exchange together with the import duty. Official reports therefore indicate that a minimum of 26,400 eligible NRI's imported 132 tonnes in 1992-93, 21,800 imported 109 tonnes in 1993-94, and 37,400 imported 187 tonnes in 1995-96. The estimated NRI import of 220 tonnes in 1995-96 would mean a minimum of 44,000 eligible NRI imports in that year.

According to reports most of the 40 to 50 eligible NRI's arriving at Kozhikode daily (15,000 to 18,000 per year) cannot even afford the tax at the rate of Rs. 22 per gram. The implication is that the NRI's referred to are merely 'carriers' of gold on behalf of other persons or organizations who have financed the imports. In effect, liberalisation has brought with it an easy route of bringing gold into India.

Gold imports by NRI's have apparently resulted in reduction of the quantity of smuggled gold by a similar amount. The gold assets in private hands in India therefore probably remain at much the same level as they would have been, had the pre-1992 position continued. The benefits arising from NRI imports are therefore the import duty collected in foreign exchange, some reduction in smuggling of gold and, presumably, the bringing into the national economy of large sums of money, as the proceeds from any sale of such gold are required to be credited only to the NRI's non-repatriable rupee account. Thus, a certain amount of 'laundering' of illegal funds held or transferred abroad is probably taking place. However, apart from any such laundering it is considered likely that clandestine sales also take place and that some of the proceeds from such sales are re-circulated, through illegal channels, to finance further imports of gold both through NRI's and smuggling.

Gold imports by NRI's have also apparently been a major factor (apart from a general stagnation in the world price during the period) in reducing the premium in the Indian market price (the difference between the Indian market price and the world price) from between 30% and 50% prior to 1992 to about 20% at the end of 1996. On this basis further liberalisation of gold imports should cause the Indian market price to recede further and unrestricted imports to bring the Indian price more or less on par with the world price. However, it should be noted that since the beginning of NRI imports in 1992 total demand (admittedly estimated) has increased in line with increased supplies. All indications are that this relative position is likely to continue.

Available indications put the estimated total demand in 1996-97 as being over 500 tonnes, of which probably about 100 tonnes will be met by recycling of ornaments, and 30 tonnes through Special Import Licenses (SIL). The fresh demand of about 370 tonnes indicates about 330 tonnes NRI imports and the smuggling of only 30 tonnes or so.

The recent drop in the world price during January and first half of February, 1997, of about 9%, from \$370 to \$337 an ounce (31.1gram), probably resulted in increased purchases and imports of gold into India by NRI's and holders of SIL. (The total drop in the world price, from \$402 in February, 1996, to \$337 in February, 1997, was thus about 16%. A complementary drop in the Indian market rate of about 6%, from Rs. 5,050 to Rs. 4,755 per 10 gram during the same 1½ months period, stimulated sales with bullion dealers liquidating stocks in anticipation of increased supplies due to the lower world price.

Since the abolition of gold control in 1990 all official action in respect of gold has been confined to fiscal measures aimed at increasing legal supplies, mainly through imports by NRI's, on the assumption that adequate imports would eventually eliminate smuggling of gold and that the Indian market rate would approximate the world price.

Need for alternative forms of investment

This continuing and increasing level of gold demand and supply underscores the imperative necessity for the Government of India to devise and make readily available some alternative, and more attractive, forms of investment. The alternative attractions would have to be strong enough to wean the general public, particularly the rural segment or a large part of it, away from the lure of gold as a convenient and safe form of savings and investment for future security.

This lure, based on the inherent properties of gold and on experience over many centuries, is deep-rooted. Alternative forms of investment must be sufficiently attractive while, at the same time, providing the same sense of security as assets in gold. The relatively constant value of gold, ease of acquisition and of pledging against loans, and of quick realisation anywhere within the borders of India, coupled with ease of transport of high value in small volume, requires any alternative form of investment to have similar attributes. One possibility is Indexed Government Bonds. These could be made to serve the purpose, provided interest rates were sufficiently high to offset inflation and guarantee a reasonable return, purchase, registration and realisation procedures made adequately simple and foolproof, and replacement made possible in the event of loss, theft and destruction of the original Bonds.

Low Indian market rates for gold stimulate purchases by the general public while high market rates are a deterrent. An alternative to Indexed Bonds could therefore be a security whose interest rates would be gold-price related and have an inverse relation to the Indian market rates over a specified period, i.e. interest rates would be higher during periods of low gold prices and lower during periods of high gold prices.

Unless and until something on these lines is made readily available to the general public, India will continue to see an increasing proportion of disposable incomes throughout the country utilised in unproductive investment (from the national economy aspect) in gold.

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