RBI’s Repatriation of Gold from UK to India

For Prelims: Forex and Gold reserve with **RBI**, Bank of International Settlements (BIS), **IMF.**

For Mains: India’s forex reserve and the role of the central bank in its management.

Source: ET

Why in News?

Recently, the **Reserve Bank of India (RBI)** has undertaken a significant strategic move by bringing back over 100 tonnes of gold from the UK to its domestic vaults.

- This has marked the largest such repatriation since the early 1990s and signifies the RBI's evolving approach to managing its gold reserves.

Note

- During the **1990-91 foreign exchange crisis,** India pledged part of its **gold reserves to the Bank of England to secure a USD 405 million loan.**
- Although the loan was **repaid by November 1991, the RBI chose to keep the gold in the UK for logistical reasons** as the gold stored abroad can be easily used for trading, entering into swaps, and earning returns.
- The repatriation of gold reserves has **no financial implications** for India's **GDP,** tax collections, or the RBI's balance sheet, as it only involves a change in the storage location of the gold (the **total gold asset of the RBI will remain the same)**.
- There are no customs or GST **implications** associated with this transfer, as the **gold being repatriated is already owned by India.**

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A Stylised Central Bank Balance Sheet

Liability	Asset
1	2
Currency	Gold
Deposits, of	Loans and advances, to
Government	Government
Banks	Banks
Loans (including securities)	Investments, in
Other Liabilities	Government securities
Capital Account	Foreign Assets
Paid-up Capital	
Reserves	Other Assets
Total Liabilities	Total Assets

How Much Gold Does RBI Have?

- **Gold Stock:**
  - The **Reserve Bank of India Act, of 1934** provides the overarching legal framework for the deployment of **reserves in different foreign currency assets and gold** within the broad parameters of currencies, instruments, issuers and counterparties.
  - As of the end of March 2024, the RBI held **822.10 tonnes** of gold, with 408.31 tonnes stored domestically and the remaining 413.79 tonnes are still held in custody with foreign institutions like the **Bank of England and the** Bank for International Settlements (BIS).
  - According to RBI as of April 2024, the **share of gold is USD 54.4 billion** in the current forex reserve **of India (USD 648.562 billion).**
- **History of Gold Purchasing:**
  - According to the World Gold Council, **RBI is among the top five central banks that are buying gold.**
  - RBI purchased **200 tonnes of gold during the global financial crisis in 2009.**
  - The RBI bought 65.11 tonnes of gold in FY 2022, 34.22 tonnes of gold in FY2023 and **19 tonnes of gold in FY 2024.**

Gold Reserves in India

- As per the **National Mineral Inventory, total reserves** of gold ore in India are estimated at **501.83 million tonnes** as of 2015.
- Largest resources of gold ore located in **Bihar (44%), followed by Rajasthan (25%), Karnataka (21%),** West Bengal (3%), Andhra Pradesh (3%), Jharkhand (2%)
- Karnataka commands around 80% of the nation's total gold output. The **Kolar Gold Fields (KGF)** in the Kolar district is **one of the world's oldest and deepest gold mines.**

Other Major Buyers of Gold

- **People's Bank of China**: It remains a significant gold buyer. According to the World Gold Council (WGC) report (released in April 2024), **China was the top buyer of gold among central banks in the first quarter of 2024.**
- **Central Bank of Turkey**: As of April 2024, the Central Bank of Turkey had purchased the **most gold (8 tonnes) year-to-date,** bringing its total holdings to 578 tonnes.
- **Emerging Market Economies:** The WGC report consistently highlights that central banks from emerging **economies are leading the gold-buying trend.**

Why did the RBI Decide to Move the Gold Back to India?

- Protection Against Inflation:
  - When inflation **is high, gold tends to hold its value well.** Unlike currencies that can lose purchasing power due to inflation, gold's historical performance suggests it can even appreciate in price during these times.
  - This provides the RBI with the **potential for good returns even in challenging economic situations.**
- **Hedge Against Geopolitical Uncertainty:**
  - The current geopolitical climate, with events like the **Russia-Ukraine war** which has triggered a **wave of sanctions on Russia by Western nations,** leading to the freezing of Russian assets held abroad might have caused some concern for the RBI to control its assets by moving them in their own wallets.
    - Gold is also seen as a safe haven during such uncertainties.
- **Diversification and Liquidity:**
  - Including gold in its reserves allows the **RBI to diversify its** foreign exchange **holdings.**
  - Gold is a **secure and liquid asset** (can be easily bought and sold on the international market at a transparent price).
  - This provides the **RBI with flexibility and additional options for managing its reserves.**
- **Strength and Confidence:**
  - It will show India's robust economic growth and its **ability to safeguard its financial assets** and indicate confidence in the Indian economy's stability.
  - This contrasts with the **1991 economic crisis** when India had to pledge gold reserves for foreign currency.
- **Storage Charges:**
  - Bringing the **gold back eliminates storage costs paid to the Bank of England.**

What is the Significance of Gold in the Economy?

- **Limited Supply & Intrinsic Value:** Unlike currencies that can be printed at will by central banks, **gold has a finite supply** due to geological limitations.
  - This **scarcity, combined with its unique physical properties** and historical significance, gives gold intrinsic value.
- **Hedge Against Inflation:**
  - Gold has historically performed well during **inflation** by holding its value well. A 2023 World Gold Council study found a **positive correlation** between **gold prices and US inflation** over 50 years. This makes gold valuable for hedging against inflation.
- **Diversification & Stability:**
  - Gold **diversifies a country's foreign reserves, reducing dependence on a single currency** and **offering stability during economic challenges.**
  - Additionally, holding gold reserves can be seen as a sign of confidence in a country's economy by international investors.
- **Jewelry & Cultural Significance:**
  - The demand for gold in jewellery remains strong globally, particularly in certain regions like India and China.
  - Additionally, gold holds **cultural significance** in many societies, further influencing its value and demand.

Historical Regime of Exchange Rate Management

- **The Gold Standard (1870-1914):**
  - Currencies were **directly tied to the value of gold.** Each country held gold reserves to back their currency.
  - Stable exchange rates made international trade easier and predictable.
  - **Drawbacks:**

        - **Limited gold supply made it difficult to expand the money supply** to meet economic growth.
        - **Countries lost gold reserves when they had trade deficits**, which could hurt their economies.
        - **Gold discoveries** or losses could **cause sudden fluctuations** in exchange rates.
- **The Bretton Woods System (1944-1971):**
    - It was established after **World War II,** and aimed to create a more stable and predictable international financial system.
    - **Key Feature**:
        - **Fixed exchange rates with the US dollar** as the reserve currency.
        - Other currencies were pegged to the dollar at a fixed rate.
        - The **US dollar was, in turn, convertible to gold at a fixed price** of USD 35 per ounce.
    - **Challenges:**
        - **The Triffin Dilemma:** As the global economy grew, the US couldn't keep up its gold reserves to support the system.
        - The US running trade deficits created doubts about its ability to maintain the gold peg.
- **The Current Scenario (Multiple Regimes - Post-1971):**
    - **Market forces of supply and demand** determine exchange rates with variety of regimes.
        - **Floating and Fixed Exchange Rates**
        - **Pegged Rates**: A country ties its currency to a single strong currency (e.g., USD) or a basket of currencies.
        - **Dollarization**: Some countries **completely abandon their own currency and adopt the US dollar** (e.g., Ecuador). Eliminates exchange rate risk but gives up control over monetary policy.
- **Special Drawing Rights (SDRs):**
    - Special Drawing Rights **(SDRs)** was created **by the IMF as a supplement to gold reserves.** It's a basket of major currencies, **not directly convertible to gold**.
    - Price of gold is determined by supply and demand in the free market, not by its connection to currencies.

Conclusion

The RBI's decision to **repatriate over 100 tonnes of gold from the UK to its domestic vaults** is a significant strategic move. It reflects the central bank's focus on logistical efficiency, diversified storage, and confidence in the Indian economy's stability. This action aligns with global trends among central banks, as they seek to enhance the security of their foreign exchange reserves during uncertain times.

Drishti Mains Question:

Discuss the rationale behind the Reserve Bank of India's (RBI) increased holding of gold reserves. Also, evaluate the importance of gold reserves for macroeconomic stability in the context of India's growing economy.

UPSC Civil Services Examination, Previous Year Questions (PYQs)

Prelims:

Q. What is/are the purpose/purposes of Government's 'Sovereign Gold Bond Scheme' and 'Gold Monetization Scheme'? (2016)

1. To bring the idle gold lying with Indian households into the economy.

2. To promote FDI in the gold and jewellery sector.
3. To reduce India's dependence on gold imports.

Select the correct answer using the code given below:

(a) 1 only
(b) 2 and 3 only
(c) 1 and 3 only
(d) 1, 2 and 3

Ans:(c)

Q. Which one of the following groups of items is included in India's foreign-exchange reserves? (2013)

(a) Foreign-currency assets, Special Drawing Rights (SDRs) and loans from foreign countries
(b) Foreign-currency assets, gold holdings of the RBI and SDRs
(c) Foreign-currency assets, loans from the World Bank and SDRs
(d) Foreign-currency assets, gold holdings of the RBI and loans from the World Bank

Ans: (b)

Q. Indian Government Bond Yields are influenced by which of the following? (2021)

1. Actions of the United States Federal Reserve
2. Actions of the Reserve Bank of India
3. Inflation and short-term interest rates

Select the correct answer using the code given below.

(a) 1 and 2 only
(b) 2 only
(c) 3 only
(d) 1, 2 and 3

Ans: (d)