Central Banks' Gold Hunt - De-dollarisation

What is the issue?

- The Reserve Bank of India has bought 50.4 tonnes of gold since December 2017.
- This signals a new effort among many central banks to reduce dependence on the US dollar and move to gold.

What is the changing scenario with gold?

- Gold prices have been stagnating around $1,260 per ounce since 2016.
- Changing cultural preferences has reduced the sale of heavy gold jewellery in markets such as India.
- However, the mine output has been increasing, and thus exerting further pressure on prices.
- This is pushing away investment demand from exchange traded funds and buyers of gold coin and bars.
- In these challenging times, gold has received support from the global central banks.

How are central banks using this?

- There was purchase of 651 tonnes of gold by global central banks and other institutions in 2018.
- Additions to central bank gold reserves spiked 74% last year.
- This is largely why the surplus in gold reduced, helping support the prices.
- **RBI** - There has been a long break since the last time the RBI added gold to its reserves in 2009, when 200 tonnes was bought from the IMF.
- But there appears to have been a change in RBI's line of thought since 2017, from when it has joined the gold buying countries.
- Particularly since March 2018, the RBI has been buying gold consistently.
- With these purchases, the country’s gold reserves have risen to 606 tonnes towards the end of February 2019.

Is this an anti-American strategy?

- There is a definite pattern apparent in the countries that are leading this central bank gold hunt and adding gold to their forex reserves.
- Countries with a strong anti-American sentiment, that wish to reduce their

dependence on the US dollar, top this list of nations.

- **Russia** - This gold buying spree has, in fact, been led by Russia and its allies.
- Russia has been steadily adding to its gold stock-pile since 2006 but the additions accelerated after 2014.
- Notably, in 2014, Russia's incursion into Ukraine flared its conflict with the US.
- One-fifth of its forex reserves are now held in the form of gold.
- Russian allies such as Kazakhstan, Uzbekistan, Tajikistan and Kyrgyz Republic are other nations that have been adding gold to their reserves over the last decade.
- **Turkey** - Relations between Turkey and the US have been steadily deteriorating since 2016.
- It was when Turkey demanded that the US extradite a cleric who was suspected of being involved in the failed coup in Turkey that year.
- Consequently, Turkey decided to bolster its war chest by purchasing 85.9 and 51.5 tonnes of gold in 2017 and 2018, respectively.
- **China** - China too has shown a growing liking for gold in recent years.
- It has purchased 454 tonnes of gold between 2003 and 2009 and another 604 tonnes between 2009 and 2015.
- As seen, all these countries are moving towards de-dollarisation and making conscious efforts to reduce their dependence on dollar.
- They are reducing their investments in US government securities and trying to settle bi-lateral trade in local currencies.

What is the emerging economies' rationale?

- Besides, the above countries, a few other central banks seem to have decided to add to the gold reserves since late 2017.
- These particularly include the emerging economies such as Poland, Hungary and India too.
- Emerging economies, including India, are nervous about future policies of the US government due to the -

    i. trade war unleashed by the US
    ii. clear anti-globalisation stand taken by the current US government
    iii. lack of respect displayed for policies that promote peace and inclusive growth

- All these have made it imperative to reduce dependence on the US currency as it can turn volatile in tandem with the U.S.'s policies.
- There is also mounting debt in the US and uncontrolled printing of notes for successive quantitative easing programmes since 2009.
- These too have eroded the intrinsic worth of the dollar significantly.

- Moreover, for now, there is no viable alternative to dollar among the currencies of other major economies.
- So this leaves gold as the only alternative avenue for global central banks that wish to divert part of their reserves away from the dollar.

What do these imply?

- The recent development with gold is beneficial for those who have stashed a large portion of their savings in the form of gold.
- It signals that gold retains its position as a premier store of value.
- [The consumption demand for gold is slowing in countries such as India.
- But it is increasing in the US, China, Hong Kong, Thailand and some countries in the Middle East.]
- The central bank buying further shows that gold will continue to be a reliable diversifier and a hedge against volatility in other currencies.
- So the accumulated wealth of households in the form of gold is unlikely to depreciate significantly.
- However, caution must be taken as the hope that money parked in gold would grow one's wealth may not be the case at this juncture, given the price scenario.

Source: Business Line

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