OUTLOOK

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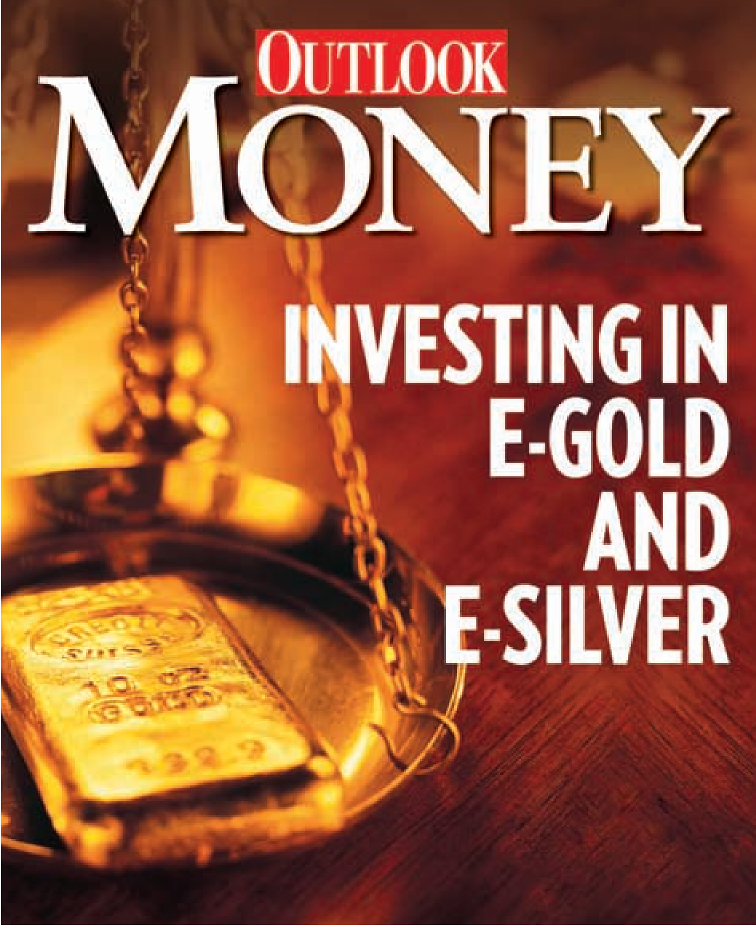

INVESTING IN E-GOLD AND E-SILVER

BROUGHT TO YOU BY

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INVESTING IN E-GOLD AND E-SILVER

E-investing is revolutionising the investment space for Indians. It is bringing in opportunities for them to participate in the growth story of commodities by allowing them to move funds into commodities in smaller denominations and holding them in the electronic, that is, dematerialised form. Its uniqueness lies in buying, accumulating, holding and liquidating commodities as well as converting them into physical units in a seamless manner.

Indians are great savers, but awful investors. Our savings ratio is at a high 29 per cent of the gross domestic product (GDP), but a meagre 6 per cent of these household savings finds its way into wealth generating equity markets, showcasing our inability to make the transition from savers to efficient investors. Our gold investing habits show a similar theme. Indians are the largest buyers of gold in the world. But, here is where we go wrong. Most of our gold purchases are in the form of jewellery. While they may look nice and make you look rich when you wear them, as a means of financial investment, they are pretty useless. The amount of charges that the jewellery passes on in the form of design and making costs are high; if you sell that necklace or ring, you will get a fraction of the price you paid for it.

INTRODUCING E-GOLD AND E-SILVER

Mass participation of retail investors in commodities is still absent. Futures contracts carry high risk and are products which few of us understand. E-gold and e-silver, launched by National Spot Exchange (NSEL), are all about investing in gold/silver in both the dematerialised and physical forms. Just as you can trade equities in the stockmarket, here, too, you can make an online transaction. On purchase, units of e-gold or e-silver get credited to the buyer's demat account; the underlying unit of physical gold/silver is stored in the exchange's vault. Looking at various parameters—ease of transaction, cost of purchase, returns and safe-keeping—e-gold and e-silver seem to be the smarter way of saving in these alternate forms of investments.

Why e-gold or e-silver?

- Holding gold or silver in demat form;
- Opportunity for retail investors to diversify portfolio;
- No worry for daily MTM pay-in/payout as in derivative buying;
- No risk of theft. Purchase in safe custody;
- Hassle-free and low-cost investing; and
- High liquidity at low costs.

INVESTING IN GOLD

Why invest in gold? Gold, a symbol of wealth, has been traditionally considered as a hedge against inflation, mostly moving in tandem with rising inflation and inversely with the dollar. Gold is a highly effective portfolio diversifier due to its low-to-negative correlation with all major asset classes. Over the last 20 years, gold has shown no statistically significant correlation with equities. The fundamental reason for this low correlation is that the factors driving gold price are not the same as the ones that determine the returns on other assets. While, as a rule, gold shows no statistically significant correlation with mainstream asset classes, there is, however, evidence that when equities are under stress—in other words, when shares are falling rapidly in value—an inverse correlation can develop between gold and equities.

The value of goods and services that gold can buy has remained largely stable, unlike currencies, which have seen significant fluctuation.

A study spanning a 400-year period has shown that the basket of goods and services that gold could buy over the period has remained the same. Gold protects your portfolio from volatility because the factors—both at the macroeconomic and microeconomic fronts—that affect the returns from most asset classes do not significantly influence the price of gold.

For a given level of returns from a portfolio, the risk or volatility can be reduced by adding gold to it. Similarly, tumultuous situations, such as a global economic crisis across countries and currencies, or even an occurrence of war, which have a negative impact on prices of most asset classes, have a positive impact on gold prices. This is because the demand for gold goes up as a safe haven for parking funds. It is the only medium of exchange completely free of credit risk as it does not imply a liability for any other entity.

The US dollar may lose its sheen amid the burgeoning US trade deficit and the country's mind-boggling borrowings to finance the same. In addition, many countries are planning to reduce their reliance on the dollar and diversify their foreign currency reserves. There certainly seems to be a trend towards increased diversification of reserve assets, away from what is seen as a dollar in decline, with gold probably being a major beneficiary.

Inflation could be another trigger which may intensify as a result of government deficits and loose monetary policies around the world. Inflation has historically been fuelling gold prices as investors seek to safeguard their wealth against rising inflation. Another factor to be noted is the introduction and growing popularity of gold exchange-traded funds (ETFs) which have changed the market in a very important way. By facilitating gold investments and ownership, ETFs have brought significant numbers of new participants into the market. These ETFs shall continue to drive gold prices higher.

COMPARISON OF INVESTMENT IN GOLD THROUGH DIFFERENT MODES

PARAMETER	JEWELLER	BANK (bars/coins)	GOLD ETF	NSEL e-GOLD
Purchase & Sale	Physical form	Physical form	Demat	Demat
Trading Timing	Shop hours	Bank hours	10 am-3 pm	10 am-11:30 pm
Buyers' Premium	High	Very high	Low	Low
Making Charges	Involved	Involved	None	None
Impurity Risk	May exist	May exist	Cannot exist	Cannot exist
Recurring Expenses[1]	High	High	Low	Low
Delivery Centre	Single	Single	Single	Multiple

WHY GOLD

The reasons why gold should form a part of your portfolio are many. Here are some of them:

- Gold improves the stability and predictability of portfolio returns. It is not correlated with other assets because gold price is not necessarily driven by the same factors that are responsible for driving the performance of other assets.
- Adding gold to a portfolio introduces an entirely different class of asset. Gold is unusual because it is both a commodity and a monetary asset.
- Gold is one of the few financial assets that is not linked to a liability. It can provide 'insurance' against extreme movements on the value of traditional asset classes.

DEMAND AND SUPPLY FACTOR

Understanding the dynamics in the bullion market is easy and difficult at the same time. The easy argument is that it is a simple economic theory of demand and supply. The complexity is that the various factors that influence demand and supply of gold are themselves dynamic. The basic fact is that gold prices are going through the roof because of high demand and stable-to-low supply.

Global demand for gold is 1,000 tonnes more than the supply. With no new mining capacity being discovered, most of the gold is being recycled. Inflationary pressures in the world economy are positive drivers of gold prices. The central banks of Russia, China and West Asian countries are giving strong buying support to gold prices. The total gold supply is fragmented into mining supply, scrap sales and central bank sales. Scrap sales are sourced from old fabricated products that have

been recovered and refined back into bars. Mine production contributes nearly 60 per cent to the overall supply side while scrap accounts for 26 per cent with the remaining 14 per cent is sold by the central banks.

According to the World Gold Council, there are more than 400 gold mines operating in the world. Gold mining is relatively inelastic and, hence, the overall level of global mine production has been relatively stable, averaging approximately 2,481 tonnes per year since 2005. This means there has not been any significant expansion in the global supply. The yellow metal has its demand spread across the world and 55 per cent of total gold demand across the globe is attributable to just five countries—India, Italy, Turkey, the US and China—though not in any particular order.

China is increasingly making its presence felt in this area and is all set to surpass India in terms of gold demand. Though, it may do so in terms of consumption, but it won't be able to surpass India in terms of imports because China is also among the top gold producing countries.

Moreover, prices have shot up because key gold producers across the world have been implementing a major dehedging exercise. It involves a gold producing company buying back its "hedged" gold in expectation of price rises. The producers are accelerating the process of buying back hedges to get full exposure to the metal in anticipation that prices will rise further.

In most industries, rising demand kicks off an increase in supply that brings prices down. But gold is often less than responsive as new supply is limited and prospects of a sudden flush of new gold are slim. There have been no new large discoveries of gold. Investment in the recent past for exploration has been insignificant. Even if a new mine is discovered, it will be about 10 years before the first ounce of gold from it sees the light of the day. The upward trend in the annual production is now levelling off. Independent analysts are of the belief that mine output will remain flat for the next few years and may even drop slightly.

INDIAN SCENARIO

The passion for gold in India has strong historical, cultural, and economic underpinnings. For centuries, gold has been equated with money, savings, riches, and status in India. India has been known to possess large stocks of gold, which are mostly accumulations from centuries of imports rather than a result of production from its own mines. Even today, domestic production only serves a small fraction of India's consumption requirements.

Globally, India is ranked sixth in the top-10 list of the gold and currency reserves: The first three positions are being held by Japan, Russia and China, respectively. India consumes anywhere between 600 to 700 tonnes of gold annually.

But domestic production of gold is only about 2 tonnes per annum. India is the highest consumer of gold mainly because of religious factors and a traditional fascination for this yellow metal. The consumption is leading to higher imports of gold as India doesn't produce enough of it to meet its requirements. India needs a huge investment in gold mining sector as it mines only 0.4 per cent of its total demand despite having 8 per cent of total world gold reserves under its land mass.

INVESTING IN SILVER

Why invest in silver? Silver has traditionally been considered the poorer cousin of gold. Most Indians who are dedicated investors in gold have shied away from investing in this other precious metal. But, with gold prices at their all-time highs and silver prices still a distance away from theirs', it's time to take another look at silver.

Silver is often compared to gold as a precious metal, but what makes it such an interesting investment is its industrial use. Largely a by-product of zinc, lead, copper and gold mines, silver has an intrinsic value because of its natural industrial demand.

While gold and silver prices have tended to follow each other over time, silver, over a long historical period, has outperformed gold (by about a percentage point annually in rupee prices).

That said, silver also has comparatively higher risk than gold. In fact, it can be considered a geared play on gold because silver prices outperform gold prices on the upside, and crash more quickly on the downside.

DEMAND AND SUPPLY FACTOR

Silver is a metal that is associated with metals such as gold, lead, zinc and copper, though its unusual properties make it very different from them. It is used in making various kinds of jewellery as it is considered a precious metal second to gold, but its contribution in the various industrial sectors as a raw material makes it unmatchable. No other metal can replace silver as it has an endless number of uses.

Silver is produced throughout the world. However, an interesting fact is that the primary source of silver is not the silver mines, but the other sources of silver. Silver mines produce a small amount of silver that is 25 per cent of the world's total production and the rest of it is derived as a by-product from gold mines (15 per cent) copper mines (24 per cent), lead and zinc mines (34 per cent) and other sources. The total production of silver in the world figures to be around 615 million ounces and Mexico is the leading silver producing country. The total demand of silver in the world amounts to around 29,000 tons.

The rally in silver prices has recently been driven by investment demand in the safe havens like the still-recovering US and Europe economies. In addition, industrial demand for silver for emerging markets is increasing the prices. Locally, the demand for silver is influenced by economic growth and the monsoons. Its prices, in comparison to gold, have been more sensitive to business cycle fluctuations, while gold, a store of value, has been less sensitive.

INDIAN SCENARIO

India hardly produces any silver and is primarily a silver importing country. It holds the 20th place in the list of silver producing countries and the total production of silver in India in 2009 was around 7.3 million ounces. Over 50 per cent share of import of silver in India is held by Chinese silver. In India, investors have limited ways to take exposure to silver. While gold ETFs are popular, asset managers are not allowed to hold silver directly in ETF or MF form, leaving investors no choice but to buy silver futures. Also, jewellery has been a big source of demand for silver and, in fact, with gold prices at their current levels, more and more Indian jewellers are increasing the amount of silver used in jewellery.

TRADING IN E-GOLD AND E-SILVER

Unlike the past, when gold could be bought either in physical form or

CONTRACT SPECIFICATIONS OF E-GOLD

COMMODITY DETAILS	
Commodity	E-gold (Demat gold units)
Contract symbol	E-gold
Daily contract	Daily contract for trading in Demat E-gold units
TRADING RELATED PARAMETERS	
Trading period	Mondays through Fridays (except Exchange specified holidays)
Trading session	10:00 am to 11:30 pm
Trading unit	1 unit of E-gold, equal to 1g of gold
Price quote/base value	Per 1g of gold of 995 purity
Tick size	10 paise per unit (min price movement)
Daily price range	5%
Maximum order size	10,000 units
MARGIN PARAMETERS	
Initial margin	5%
Delivery margin	10%
DEMAT PARAMETERS	
ICIN	INC200000007
Market description	T+2
Settlement cycle	T+2
DELIVERY RELATED PARAMETERS	
Delivery unit	1 unit and multiple thereof
Quality specifications	Grade: 995 and Fineness: 995 Only dematerialised units eligible
Tender and delivery day	T+2 (two working days from the date of transaction)

CONTRACT SPECIFICATIONS OF E-SILVER

COMMODITY DETAILS	
Commodity	E-silver (demat silver units)
Contract symbol	E-silver
Daily contract	Daily contract for trading in demat e-silver units
TRADING RELATED PARAMETERS	
Trading period	Monday To Friday (except Exchange specified holidays)
Trading session	10:00 am to 11:30 pm
Trading unit	One lot of 100 demat units of e-silver, equivalent to 100g of silver
Price quote/base value	Per 100g of silver of 999 purity
Tick size (min. price movement)	10 paise per trading unit
Daily price range	5%
Maximum order size	50,000 units
MARGIN PARAMETERS	
Initial margin	5%
Delivery margin	10%
DEMAT PARAMETERS	
ICIN	INC200000015
Market description	T+2
Settlement cycle	T+2
DELIVERY RELATED PARAMETERS	
Delivery unit	1 lot (equal to 100 demated units)
Quality specifications	Grade: 999 and Fineness: 999 Only dematerialised units eligible
Tender and delivery day	T+2 (2 working days from transaction)

through gold ETFs, now one can buy and sell gold electronically. Trading in e-gold and e-silver can happen on the terminals of any authorised dealer permitted to trade in e-gold and e-silver on your behalf. For example, in the equity market, it is settled on T+2.

SPECIFICATIONS

Understanding of the contract details, procedure of settlement, dematerialisation and delivery of physical gold and silver against surrender of demat units is important for every investor, authorised dealer or participant in the trading of e-gold and e-silver. See pages 16-17 for some of those contract specifications while buying and selling of the units.

OPENING OF DEMAT ACCOUNT

One needs to open a demat account for initiating any trade to buy gold or silver online. The Demat account in the name of an individual can either be on single or joint basis and would be used by the accountholder for holding and transacting in demat units in electronic form. It can also be opened in the name of a corporate, HUF, a society or a trust. One can open this account either in NSDL or CDSL. A depository account is a demat account opened by a trading-cum-clearing member or any other clearing member of the exchange. This account is maintained by the member to receive and deliver demated units from/to the exchange against obligation of the clients operating through such member. A pool account is exchange-specific. Exchange effects the pay-in and pay-out through such pools accounts in both depositories.

BUYING AND SELLING MECHANISM

Buying. Investing in e-gold and e-silver is as simple as buying equity shares. Clients desirous of buying any quantity of gold or silver need to transfer sufficient money to their respective broker before placing the order. Once the money is transferred, one needs to call the broker and place the order. After the order's execution, gold/silver is transferred to client's demat account in T+2 days (e.g., if you buy on Monday, you get the delivery on T+2 days, i.e., Wednesday in your demat account).

Selling. If a client wishes to sell his holdings, he should transfer it to the broker's designated account. After a successful transfer of holdings to the broker's account, he would need to call the broker and place the sell order. After the order's execution, funds are transferred to the client's trading account in T+2 days.

PAY-IN AND PAY-OUT DAY

When a client having demat holding in his beneficiary account wants to sell, he can approach any member of NSEL and, accordingly, transfer the bullion to the member's pool account on or before the pay-in deadline. On receipt of the same in pool account, the selling member shall issue Delivery Out (DO) instructions to the exchange before the deadline. While filling up the account transfer form, the client should ensure that all the details as mentioned below have been correctly entered and all the holders have signed the form:-

ICIN. This will be available in the demat holding/statement.

Quantity. This is the number of units sold by the client. The client should ensure that he is in possession of such units on the date of execution.

Execution date. The date on which the client intends to transfer his units to the CM pool account of the respective member.

Market type and settlement number. This is made available by the exchange through a circular, which is issued every month. The client can also get the same from his broker or DP.

The client should submit the form to his DP and take an acknowledgement for the same. The DP shall execute the transfer instruction and transfer the bullion from the client's account to the respective member's pool account.

The member is also required to ensure that it has received all the deliveries from his clients before the scheduled pay-in time. The member shall also ensure that he has transferred the same to the exchange before the pay-in deadline. On T+2, the exchange will declare pay-out of units. The exchange will transfer demat credit into the CM pool account (NSDL/CDSL) of the respective members equivalent to their net buy

position. The member, in turn, will transfer demat credit to the respective client's beneficiary accounts. The exchange will receive/transfer units on net basis. The member will be required to get transfer of units from other selling clients and to transfer units to all buying clients so as to ensure discharge of total delivery obligation at client level.

OPTION TO TAKE PHYSICAL GOLD OR SILVER

If the unitholder is interested in taking physical delivery of gold or silver bar/coin against his units, he can surrender such units to the exchange and get physical delivery, at any point of time at his discretion, subject to the conditions. Delivery of physical gold or silver bar/coin is offered in specified lots/denominations and at specified locations only, where the exchange has made vaulting and delivery arrangements. Presently, gold is made available in multiples of 8g, 10g, 100g and 1kg and any combination thereof, while silver is made available in multiples of 100g, 1kg, 5kg and any combination thereof.

Currently, delivery of physical gold and silver is made available at

TRANSACTION CHARGES

WHILE ENTERING INTO A CONTRACT, IT'S IMPORTANT TO UNDERSTAND THE VARIOUS CHARGES AND THEIR APPLICABILITY CURRENTLY

TRANSACTION CHARGES	The exchange shall levy the turnover charges ₹10 per lakh of turnover to both buyer and seller member on monthly basis. This shall be applicable on all executed transactions
DEMATERIALIZATION /CORPORATE ACTION CHARGES	The authorized dealer will be charged at such rate as may be levied by NSDL from time to time.
STORAGE CHARGES	No storage charges.
DELIVERY CHARGES	In respect of buying and selling of e-gold and e-silver units resulting into demat deliveries, the exchange will not levy any delivery charges. In respect of lifting of commodities, the exchange shall levy the delivery/lifting charges and will charge a total of ₹200 per lifting for gold and ₹150 for silver, irrespective of number of coins/ bars involved in the delivery instruction.
OTHER CHARGES	In addition to the charges imposed by DP and depository, the exchange shall levy the charges on account of cost of making, packaging and refinery certification charges. In addition to these charges, the client opting for conversion will be required to pay VAT/GST, other local taxes, and octroi, if any, applicable at the place of delivery as may be applicable on the date of execution

Delhi, Kolkata, Chennai, Hyderabad, Jaipur, Mumbai and Ahmedabad. The exchange will keep on expanding the number of centres in future to offer physical delivery. If a client opts for physical delivery, he can get it from any centre of his choice out of such specified centers.

For the purpose of physical delivery, the client needs to submit a delivery instruction slip (DIS) to the DP along with the Surrender Request Form (SRF) and authorisation letter so as to transfer the intended number of units to the following accounts of NSEL. The DP thereafter shall transfer the units to the account of NSEL based on DIS. The DP should also attest the signature of the holder on the Surrender Request Form, authorisation letter, ID proof and hand them over to the client along with the acknowledgement of DIS slip.

The unitholder shall submit DIS and SRF to the exchange, specifying the centre of his choice from where he intends to take delivery. On receipt of the copy of DIS and SRF, the exchange shall compute charges relating to making and packaging charges of coin/ bar, delivery charges, VAT and other dues, if any.

The exchange will communicate the total amount due to the respective client through the email ID provided in the SRF. After collecting the payment, the vault will hand over delivery of gold/silver to the respective investor.

It's widely believed, and not without reason, that the value of gold and silver will reach new heights in the times to come. There are good enough fundamental and technical reasons to support this view. Therefore, just as you have a combination of equity and debt asset classes in your investment portfolio to meet your long-term goals, gold and silver, too, deserves a pride of place. **II**