Superiority of Gold Bonds over Gold ETFs

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Abstract : **Gold is considered as a famous asset class. In India, Gold is attached with emotions and sentiments of the people. Most of the Indians hold physical Gold with themselves in the form of jewellery and ornaments rather than considering it as an investment avenue. Investment in Gold can be made in variety of alternatives like physical Gold, Gold Bonds, Gold ETFs, Gold Deposits and Gold funds etc., Sovereign Gold bonds are the long term debt instruments issued by the Reserve Bank of India on behalf of the Government of India which provides Gold investor, an interest rate of 2.5 percent annually. Gold ETFs are other form of Gold investment that tracks the market prices of physical Gold. Gold ETFs and Sovereign Gold bonds are paper form of Gold investment without taking the risk of delivery and storage. The present paper is a study on comparison of the performance of Gold Bonds and Gold ETFs. Gold bonds looks attractive over Gold ETFs as they are providing 2.5 percent fixed rate of interest annually and there is no entry load or exit load.**

Keywords: **Sovereign Gold bonds, Gold ETFs, Physical Gold, Gold investment, Gold Deposits**

I. INTRODUCTION

A gold bond is a Government security. Gold bonds were first issued in India in the year 2015 as a part of Government Gold schemes. Government of India aims to convert the physical Gold demand into paper Gold to reduce the imports of Gold. Gold bonds track the prices of physical gold. Each unit of gold bond backs price of 1gram of gold. Gold bonds can be bought from the primary market and also from the secondary market as they are listed further in stock exchanges for trading.

1.1 Features of Gold bonds

- The bond provides a fixed interest rate of 2.50% semi annually.
- Returns of Gold bonds are in line with prices of gold.
- Gold Bonds provide sovereign guarantee on principal amount and interest.
- Minimum investment in gold bond is one gram and maximum limit of investment is 4 KGs for individual, 4 KGs for HUFs. For trust and similar entities, the limit is set as 20 KGs per fiscal year.
- Gold bonds available in paper form and De-materialisation form
- Gold bonds are listed on stock exchanges and trades like an equity share.

1.2 Advantages of Gold bonds

- Gold bonds are secured. There is very less risk of holding and no storage charges unlike physical gold.
- Provides 2.50% fixed interest annually on the initial investment
- Gold bond prices are linked to prices of gold of 999 purity (24 carat) published by IBJA.
- Sovereign Guarantee is provided on redemption amount and interest amount.
- The tenure of the gold bond is for 8 years with a lock in period of 5 years.

- All issuance of Gold bonds are trading on National Stock Exchanges.
- Sovereign gold bonds can be considered as security/collateral for loans.

1.3 Tax benefits of investing in gold bonds

- Gold bonds are exempt from capital gains tax if held till maturity unlike gold ETF, gold funds or physical gold. The maturity period is eight years.
- No GST on gold bonds, whereas 3% GST is levied on purchases of gold. Gold bonds are also free from issues like making charges. It is backed by the government of India and allows subscribers to own 24 Karat gold.
- Gold bonds pay interest at 2.5% annually and the interest income is clubbed with the subscriber’s income and taxed accordingly. But the interest income does not attract tax deducted on source

Gold Exchange Traded Funds are investment alternatives for gold investors without taking delivery of physical gold. Prices of Gold ETFs track closely the prices of physical gold. Gold ETFs allow investors own gold in their De-mat account. One unit of the Gold Exchange Traded Fund lets the investor own 1gram of gold without physically owning it. Today, few gold investment companies are offering gold ETF units at one hundredth of a gram for liquidity and marketability which is a limitation of buying physical gold. Gold ETF is liquid because one can trade in it at any time during market hours. Gold ETF provides marketability as it is trading in the stock market like an ordinary share. Investor can short sell a gold ETF unit and also he can buy it on margin. Owning gold ETF is cheaper than owning physical gold because it has no cost of carry and costlier than Gold bond as it has entry and exit loads and maintenance charges.

Gold ETFs are usually sold by mutual fund distributors. These are marketed to high net worth and retail individuals, but mostly in large cities. On the other hand, the gold bonds may be available through post offices and banks, which will help in reaching out to retail investors even in smaller towns and villages.

1.4 Objective of the study

1) To compare the performance of sovereign Gold Bonds and Gold ETFs.

II. METHODOLOGY

The study is an empirical study based on secondary data. The data has been collected from various published sources and websites. Data for gold ETF has been taken from the website of NSE and data for sovereign gold bonds are collected from the sources like reports from RBI, Business Standard, HDFC Retail research and Economic Times.

III. REVIEW OF LITERATURE

Sudindra VR , Gajendra Naidu Jatty (2019) Concludes that the Sovereign Gold Bond has advantages in the following parameters viz; regular returns, safety& purity of gold, holding period return, purchase value, capital gain, collateral to avail loan, storage cost, when compared to physical gold, gold ETF, Gold coin and gold jewellery.

Anu Anna Ninan (2018) explained in his paper "*Sovereign Gold Bond Scheme –An Alternative to Physical Gold Investment in Kerala"* that the sovereign Gold bond is a new alternate for investment in gold. Author of the paper also suggested making the gold bond scheme popular through public awareness.

Amar G, Satijani, Dr. Jaspal Gidwani, Avinash Sahu (2018) Concludes that the Sovereign Gold Bond has advantages in the following parameters viz; 2.50% annual interest rate, transaction charges, sovereign guarantee, credit risk, total expense ratio, when compared to gold ETF.

Rishabh Gupta (2018) in his paper identifies that the awareness of Sovereign Gold Bond scheme among the investors is still very moderate. Many investors still believes physical gold as a safer option irrespective of interest government may provide. There is still lack of income tax clarity on few provisions of SGB..

CA Rashmi Chaudhary and Priti Bakshi (2016) have compared Gold Monetization scheme and gold bond scheme. The results of the study reveal that the gold bond scheme performed much better than Gold Monetisation Scheme.

Adhana (2015) in her paper explained the probable impact of sovereign gold bond scheme on current account deficit. The paper also highlighted certain steps for the successful implementation of gold schemes. Better policy implementation, stabilising gold market, infrastructure and human resource development, etc are some of the steps which help in accelerating the growth of SGB scheme.

M Avabruth (2015) referred in his study that the sovereign gold bond is the preferred investment in gold after physical gold and Gold ETFs. Gold bonds provide good return and safety than other forms of gold investments as they are backed by the Government. Emotional attachment of investors plays a major role in success of Gold bonds.

G Venkatachalam, Dr.G Prabakaran (2015) in their paper, "A study on investors' behaviour towards Gold Exchange Traded Funds in Indian stock market with special reference to Tamilnadu" concluded that the factors like investment frequency, preferred risk level, and information sources makes investor invest in gold ETFs.

Jalpa Thakkar, Sheenam Gogia, Vatsala Manjunathan (2013) concluded that the investors were already known about the returns of gold and they plan to invest more on gold. Study also points lack of awareness about other gold investment alternatives like e-gold, gold funds, fund of funds, gold ETFs.

IV. DATA ANALYSIS

To compare the performance between Sovereign Gold Bonds and Gold Exchange Traded Funds (GETFs), four Gold ETFs from NSE, IDBI Gold ETF, AXIS Gold ETF, KOTAK Gold ETF and Birla Sun Life Gold ETF closing prices were used. Returns of the ETFs are determined from 1st January 2019 to 31st December 2019 and 1st January 2020 to 31st October 2020. During the same period, four tranches of Sovereign Gold Bonds, SGBDEC2512, SGBDEC25XI, SGBNOV25VI, SGBNOV25XI closing prices from NSE were observed and calculated their historical returns for comparison.

TABLE I

RETURNS OF SOVEREIGN GOLD BONDS AND GOLD ETFS IN THE YEAR 2019

Name of the Gold Bond	Return Percent	Name of the Gold ETF	Return Percent
SGBDEC2512	30.2	IDBIGOLD ETF	21.3
SGBDEC25XI	27.6	AXISGOLD ETF	22.5
SGBNOV25VI	35.6	KOTAKGOLD ETF	22.5
SGBNOV25IX	29.1	BSL ETF	17.5

Note. Data has been analysed for Gold Bonds and Gold ETFS and returns are comparatively higher for Gold Bonds in the year 2019

TABLE II

RETURNS OF SOVEREIGN GOLD BONDS AND GOLD ETFS IN THE YEAR 2020 FROM JANUARY TO OCTOBER

Name of the Gold Bond	Return percent	Name of the Gold ETF	Return percent
SGBDEC2512	33.13	IDBIGOLD ETF	29.43
SGBDEC25XI	32.91	AXISGOLD ETF	27.38
SGBNOV25VI	37.36	KOTAKGOLD ETF	29.30
SGBNOV25IX	35.98	BSL ETF	29.09

Note. Data has been analysed for Gold Bonds and Gold ETFS and returns are comparatively higher for Gold Bonds in the year 2020.

4.1 Chart showing comparison of closing prices of IDBI gold ETF and SGBDEC2512 gold bond in 2019

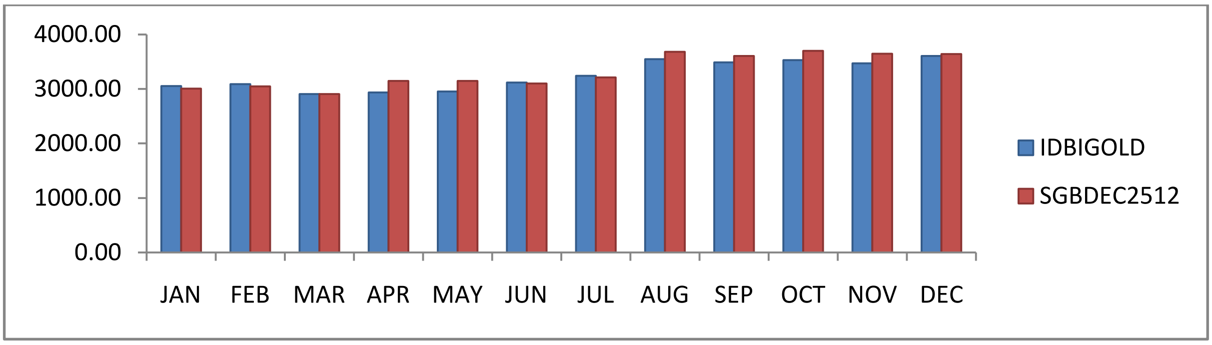

Fig. 1 **Comparison of IDBI Gold ETF and Sovereign Gold Bond (SGBDEC2512) Monthly closing Prices in the year 2019**

Closing prices of IDBI Gold ETF and SGBDEC2512 Gold Bond are compared from 1st January 2019 to 31st December 2019. From the above column chart, it can be seen that the prices of Sovereign Gold Bond closes higher during the study period.

4.2 Chart showing comparison of closing prices of IDBI gold ETF and SGBDEC2512 gold bond in 2020

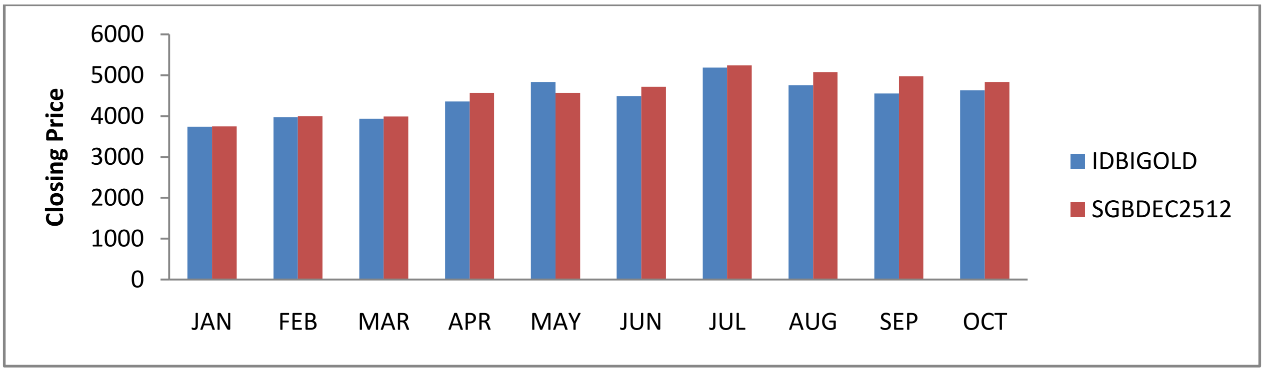

Fig. 2 Comparison of IDBI Gold ETF and Sovereign Gold Bond (SGBDEC2512) Monthly Closing Prices in the year 2020

Closing prices of IDBI Gold ETF and SGBDEC2512 Gold Bond are compared from 1st January 2020 to 31st October 2020. From the above column chart, it can be seen that the prices of Sovereign Gold Bond closes higher during the study period except in the month of May.

4.3 Chart showing comparison of closing prices of AXISGOLD gold ETF and SGBDEC25XI gold bond in the year 2019

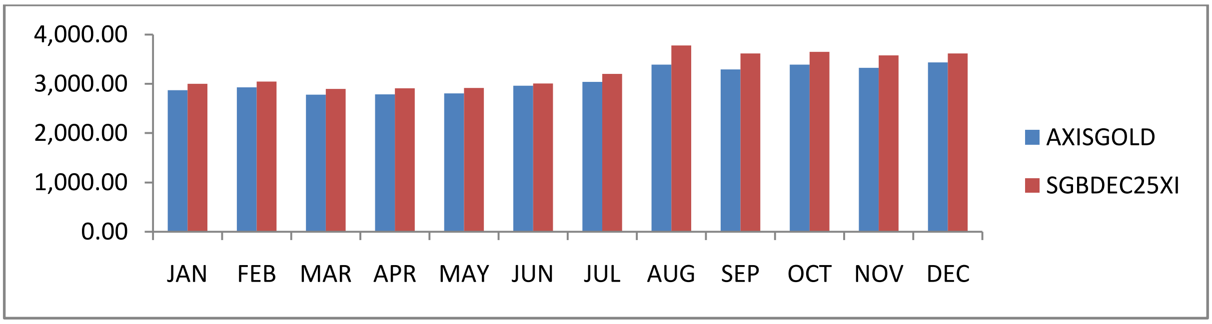

Fig. 3 Comparison of AXIS Gold ETF and Sovereign Gold Bond (SGBDEC25XI) Monthly Closing Prices in the year 2019

Closing prices of AXISGOLD Gold ETF and SGBDEC25XI Gold Bond are compared from 1st January 2019 to 31st December 2019. From the above column chart, it can be seen that the prices of Sovereign Gold Bond closes higher during the study period.

4.4 Chart showing comparison of closing prices of AXISGOLD gold ETF and SGBDEC25XI gold bond in the year 2020

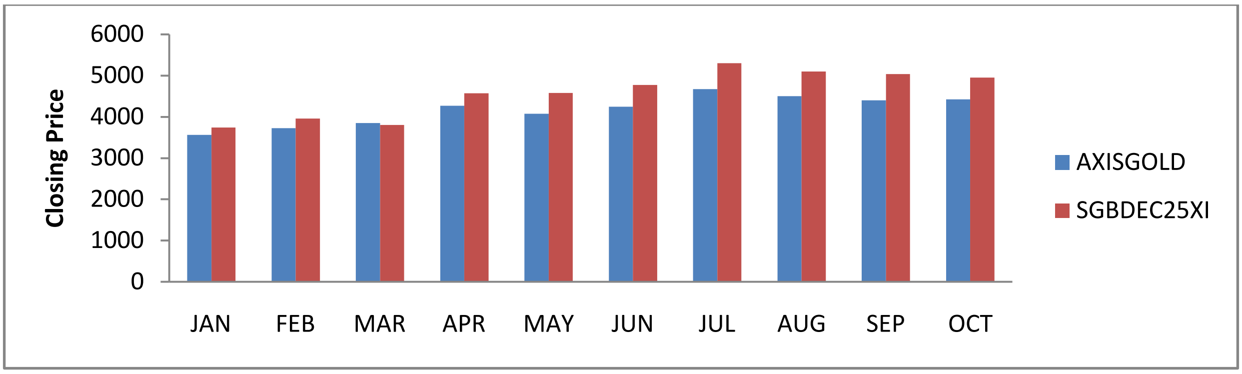

Fig. 4Comparison of AXIS Gold ETF and Sovereign Gold Bond (SGBDEC25XI) Monthly Closing Prices in the year 2020

Closing prices of AXISGOLD Gold ETF and SGBDEC25XI Gold Bond are compared from 1st January 2020 to 31st October 2020. From the above column chart, it can be seen that the prices of Sovereign Gold Bond closes higher during the study period except in the month of March.

4.5 Chart showing comparison of closing prices of KOTAKGOLD gold ETF and SGBNOV25VI gold bond in the year 2019

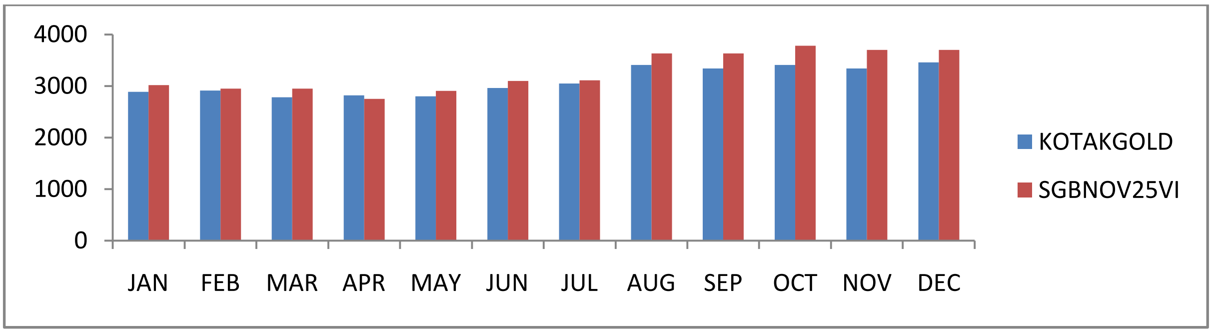

Fig. 5 Comparison of KOTAK Gold ETF and Sovereign Gold Bond (SGBNOV25VI) Monthly Closing Prices in the year 2019

Closing prices of KOTAKGOLD Gold ETF and SGBNOV25VI Gold Bond are compared from 1st January 2019 to 31st December 2019. From the above column chart, it can be seen that the prices of Sovereign Gold Bond closes higher during the study period.

4.6 Chart showing comparison of closing prices of KOTAKGOLD gold ETF and SGBNOV25VI gold bond in the year 2020

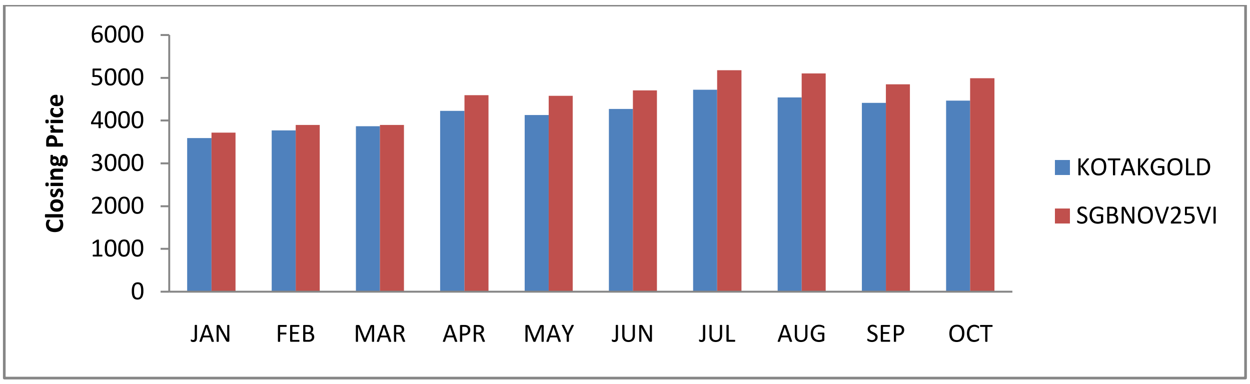

Fig. 6 Comparison of KOTAK Gold ETF and Sovereign Gold Bond (SGBNOV25VI) Monthly Closing Prices in the year 2020

Closing prices of KOTAKGOLD Gold ETF and SGBNOV25VI Gold Bond are compared from 1st January 2020 to 31st October 2020. From the above column chart, it can be seen that the prices of Sovereign Gold Bond closes higher during the study period

4.7 Chart showing comparison of closing prices of BSL gold ETF and SGBNOV25IX gold bond in the year 2019

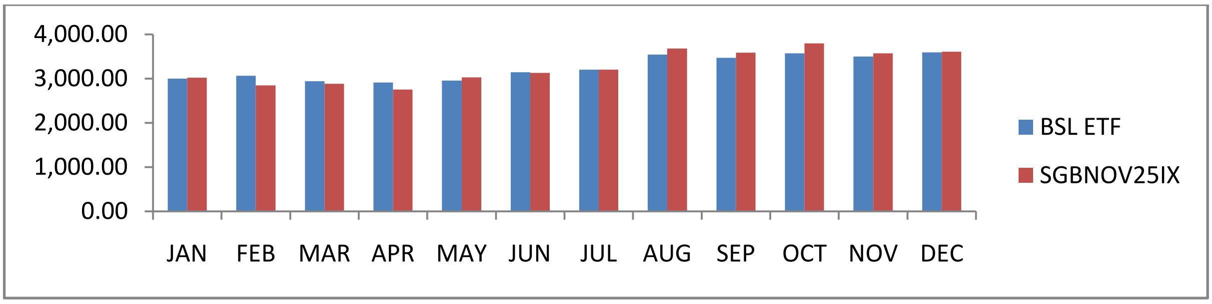

Fig. 7 Comparison of BIRLA SUNLIFE Gold ETF and Sovereign Gold Bond (SGBNOV25IX) Monthly Closing Prices in the year 2019

Closing prices of BSLGOLD Gold ETF and SGBNOV25IX Gold Bond are compared from 1st January 2019 to 31st December 2019. From the above column chart, it can be seen that the prices of Sovereign Gold Bond closes higher during the study period

4.8 Chart showing comparison of closing prices of BSL gold ETF and SGBNOV25IX gold bond in the year 2020

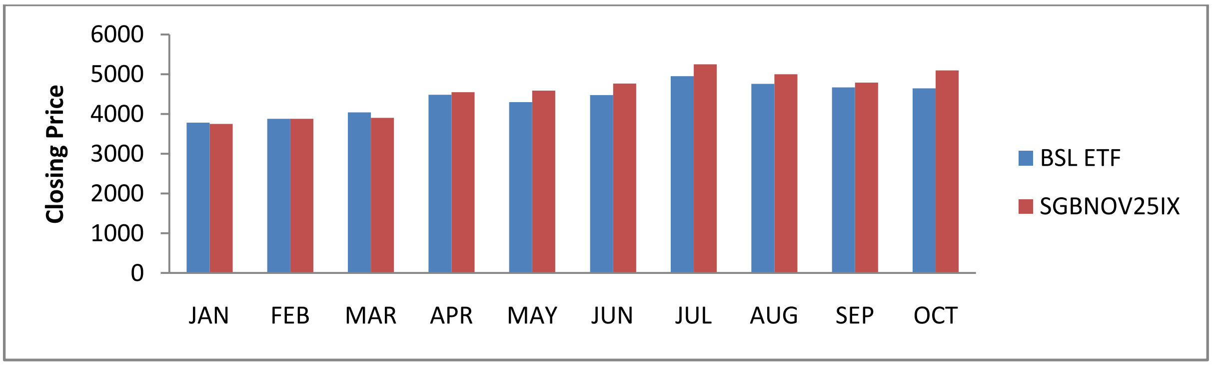

Fig. 8 Comparison of BIRLA SUNLIFE Gold ETF and Sovereign Gold Bond (SGBNOV25IX) Monthly Closing Prices in the year 2020.

Closing prices of BSLGOLD Gold ETF and SGBNOV25IX Gold Bond are compared from 1st January 2020 to 31st October 2020. From the above column chart, it can be seen that the prices of Sovereign Gold Bond closes higher during the study period except in the month of March.

Result: it is evident from the above analysis that the closing prices of Sovereign Gold Bonds closes higher than Gold ETFs more than 20 months out of 22 months of study period which clearly proves the superiority of Sovereign Gold Bonds over Gold Exchange Traded Funds.

TABLE III

COMPARISON OF SOVEREIGN GOLD BONDS WITH GOLD ETF

Factors	**Gold Exchange Traded Funds**	**Sovereign Gold Bonds**
Returns	Lesser return than return on gold	2.5 % additional interest than appreciation of gold
Safety	High	Highest
Purity of Gold	99.5 fineness gold	99.5 fineness gold.

Capital Gains Tax	LTCG applicable after 3 years	LTCG applicable after 3 years. No Capital gain tax if held till maturity
Security/Collateral against Loan	Not possible	Can be used as Collateral
Cost	Expense ratio	Nil
Tradability of Instrument	Can be tradable on stock exchanges	Can be tradable on stock exchanges
Lock- in	Not applicable	5 years
Interest payout	Not applicable	2.5% per annum
Storage Cost	Very Low	Very Low
Buying Limit	Minimum 1 gram and no upper limit	Minimum 1 gram and maximum 4 kg per person and 20 kg per trust.
Tax Implication	LTCG tax of 20 % is levied on capital appreciation after 3 years.	No LTCG tax on redemption. LTCG tax of 20 % is levied on capital appreciation after 3 years. Interest income taxed at applicable slab rate.
Drawback	Low volume on a trading platform.	Low liquidity

Note. In comparison of Gold Bonds and Gold ETFS, many factors are compared to study the superiority of the two instruments.

V. CONCLUSION:

Gold ETFs exist in India from 2007 and gold bonds were introduced in the year2005. Gold bonds are relatively new to the gold investors in India. Both the instruments are paper form of gold and cost effective. There is no risk of physical holding as they are available electronically through De-mat account. During the period of pandemic Covid-19, Gold ETFs recorded consecutive positive net inflows. During the study period, the returns of Sovereign Gold Bonds outperform the returns of Gold ETFs as these bonds are providing 2.5% of additional fixed rate of interest on investment value. The maintenance charges of gold bonds are very less compared with gold ETFs. Due to the factors like sovereign guarantee, interest income and less maintenance charges, sovereign gold bonds looks superior and attractive to the gold investors when compared with Gold ETFs.

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