

GOLD LOAN MARKET IN INDIA

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ABSTRACT

In the Article, Author tries to highlight the Gold Loan Market in India. In India, it is estimated that most of the gold is held by people in rural areas where, often, it is the only asset people have in their possession though in limited quantities. A rural Indian knows that if his crop fails or his family is sick, he can raise cash at short notice from the goldsmith or pawnbrokers and moneylenders. Gold has a formidable part in showcasing Indian customs and traditions. Women richly clad in gold jewellery are a familiar sight in Indian tradition and is a sign of prosperity and well being in a society. Also, in a rich social heritage filled with celebrations and gaiety, gold jewellery was always esteemed and in demand. Gifting of gold on auspicious occasions is also a common tradition in the country. The study is conducted to understand the gold loan market in India and its impact and gold loan and financial inclusion. The study aims at collecting information regarding the nature, character and composition of gold loan business in India, its socioeconomic impact and problems associated with the sector.

INTRODUCTION

Till a few years back, gold loans were the last resort for borrowers but the scene is fast changing with more jewellery owners viewing it as an asset to get smart loans. With the entrance of non-banking financial companies (NBFCs) in the picture, loan against gold has become all the more popular. Gold loans are amongst the newest class of assets which have seen rapid growth in securitization. The government views gold loans as an effective means of meeting the demand for micro-finance in India. Gold loans have become a basis for creation of new financial products such as loans for purchase of gold wherein gold is purchased on the date of loan and held as a pledge until the equated monthly installments are paid. The present paper tries to gain an understanding about the Indian gold loan market. Indian households typically have an emotional attachment and sense of personal belonging to the gold they own, which is usually in the form of jewellery, coins or bars. According to the World Gold Council, India accounts for 10 per cent of world's total gold stock, of which rural India accounts for 65 per cent of the total gold stock. Gold jewellery provides immense consumer satisfaction and also serves as an appreciating asset—a rare, socially valuable combination. There has been a high demand for gold in India, irrespective of prices. Traditionally, gold loans were provided only by informal market players, however, over the last few decades, there has been a considerable shift in this scenario as a pool of specialised financial institutions called NBFCs have emerged catering to the financial needs of low-income households. Gold loan is a simple modification of the age-old practice by money lenders and has been institutionalised by the banks now. In this loan, one has to deposit the household gold in the form of jewellery with the bank or financing agency and get a loan up to 60 per cent of the gold deposited. It requires proper documentation such as submission of election card/Aadhar card as identity proofs and PAN cards for income proof.

OBJECTIVES

The objectives are

- To examine the scope of gold loans in India.

- To understand the advantages of Gold loan
- To analyze the future of gold loans in India

KEY DRIVERS OF GOLD LOAN MARKET IN INDIA

The prevalence of high level of rural indebtedness, easy availability of gold loans on extremely flexible terms, relative scarcity of personal and retail loans from the banks, and changing attitude of customers to gold loans have contributed to the sharp growth in the gold loans outstanding. It was also realized that there is potential to expand gold loans market to the Northern and Western regions of India, provided the branch network is expanded and the loans are available with ease and with flexible options. Several large finance companies started expanding their branches in these regions and the response appears to be favourable. The gold loans NBFCs and banks operating in the gold loans segment have different approaches and philosophy which can be seen in the margins and profitability for different category of lenders. Gold loans NBFCs view gold loans as their most focussed business and, therefore, have built their service offerings through investment in technology and innovative practices. They have been commanding premium yields and higher profitability. In contrast, banks focus on gold loans for agriculture as a safer means to meet their priority sector lending targets, which otherwise offer low returns with high defaults. Further, even for non agriculture gold loans, their target clientele is the more high-value segment, given that they are unable to offer the level of flexibility and rapid disbursals like the specialised NBFCs.

ADVANTAGES OF GOLD LOANS

Gold loan is a secured loan- where gold ornaments, bullions or coins are kept as a security. This loan can be used for any number of purposes but towards the commission of any illegal activity or speculation in the share market. NBFCs have fewer restrictions on the purpose of the loan. The loan applicant does not have to disclose his income or salary. It can be availed by non-working individuals too. The loan is disbursed quickly and with less documentation involved so it can be utilized for immediate purposes. Disbursal through NBFCs spans a couple of minutes while those from banks may require a maximum of one or two days. Gold loans have a higher Loan-to-value ratio. NBFC's offer up to 95% of the purity of the gold while banks restrict themselves to a maximum of 75% of the purity. There is no minimum tenure. If need be, it can be paid the very next day. Average loan period varies from 90-100 days. The interest rate varies according to the tenure and amount of loan. In the case of NBFCs it is higher, around 25% whereas it can be around 12-15% in the case of banks. Rates of interest are reasonable where the LTV rate does not exceed 50-60%. Repayment can be made in one lump or it can be in done in installments.

TRENDS IN GOLD LOANS OUTSTANDING

Gold as an asset is liquid and can be readily exchanged for cash even in the informal market. With the gold market getting more organized within a formal setup, in recent years there has been rapid growth in the gold loans market particularly in gold loans disbursed by Banks and NBFCs. Both demand and supply side factors have played important roles in bringing about this growth. From the demand side, holders of gold were able to get cash in lieu of their gold in a formal setup and at higher loan to value ratios at relatively lower rate of interest under more favourable terms and conditions when compared with the informal segment. From the supply side, banks and NBFCs were able to disburse loans against collateral whose market value was going up or stable even in times of financial turmoil.

GOLD LOAN MARKET IN INDIA

With the rising demand, people also buying gold as the value of gold assets is rising continuously. On this solid base, the gold loan industry has huge potential to grow even further as currently it is estimated that less than 2% of the total gold stock is used for pledging/ obtaining gold loans. Gold loan business has existed in society since earlier times but the market was totally unorganized as there was no involvement of government or private institutions. With the entry of organized players like banks and non-banking finance companies (NBFCs), the market scenario has changed significantly and organized players grew rapidly. However, even today, there is a dominance of the unorganized sector which accounts for nearly three-fourth of the total gold loan market in the country. India has the largest gold stock in the world, i.e. more than 18,000 Metric Tons of gold held by the Indian households. The country accounts for approximately 10% of the total world gold stock in 2010. This makes the country, one of the largest gold markets and the demand for gold is rising continuously. The cumulative annual demand for gold in India will increase from the present level of 1,000 Metric Tons to more than 1,200 Metric Tons by 2020. Rural India is having the

major chunk of this gold and account for around 65% of the total gold stock in the country. Regionally, the demand for gold varies with highest demand in the Southern India, followed by West, North and East³. Similarly, the regional distribution of gold loan portfolio displays almost the same pattern with southern India recording the highest share in gold loan market. Indian households have an emotional attachment to family gold, be it in the form of jewellery, coins or bars. The gold owned by them is liquidated only in conditions of extreme financial need. Pledging of gold coins, jewellery etc to local pawnbrokers and money lenders has been prevalent in India from times immemorial. This is more prevalent in rural India as they account for the major chunk of gold stock in the country. Pawnbrokers and money lenders provide the money by securing gold assets as collateral. In earlier times, most of the gold loans were provided by the unorganized players like local pawnbrokers and money lenders. Over the past decade, the scenario has changed with the entry of banks and NBFCs i.e. organized players, who have started issuing loans against gold. However, these gold financing companies are largely providing services in the urban areas. The urban population has realized the potential of gold and has started using the same to meet their liquidity needs. This has led to the growth in the organized gold financing market. In addition, there is a huge potential for growth as only 1.3% of the total gold stock in India is used for gold loans. Due to high stocks, the rural market is the high potential area and firms need to develop strategies to develop this segment effectively and provide better accessibility to borrowers. The key players in the gold finance industry in India include the organized sector (i.e. banks/public/private/co-operatives and NBFCs) and the unorganized sector, comprising local pawnbrokers and moneylenders who have traditionally dominated the gold loan market for many decades, and who still command more than two-third of the market. The organized gold loan market stood at INR 510 Billion in FY 2011 and is expected to grow at a CAGR of around 25.5% during FY 2012-2015 to reach INR 1,285 Billion by the end of FY 2015. Besides this, gold loans gave rise to new financial products such as loans for purchase of gold, wherein gold is purchased on the date of the loan and held as a pledge until the equated monthly installments are paid. Gold savings schemes are also emerging, wherein the customers pay regular cash flows which on maturity are added with a certain amount of interest payment to purchase gold for customers.

ORGANIZED AND UNORGANIZED GOLD LOAN MARKET

With major chunk of the population living in rural India and having the largest part of the country's gold stock, the share of unorganized players is high in the Indian gold financing market. Moreover, the perspective of Indian households is different for gold financing as they consider it as an asset or personal belonging which should be used only during major financial crisis in the family. However, the scenario has been changing as people begin to realize the value of gold as an asset that can be pledged to meet short-term liquidity needs. The introduction of gold loan facility in the organized sector by banks and NBFCs, in which people have greater confidence, has further helped in changing attitudes to gold loans. Consequently, the organized gold loan market began growing at a rapid pace and many new players entered in the market.

SHARE OF ORGANISED AND UNORGANISED GOLD LOAN MARKET

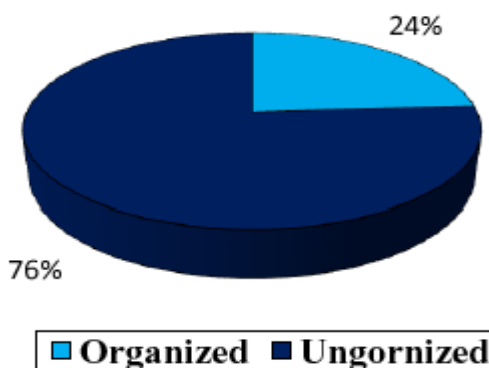


Figure 1

RECENT DEVELOPMENTS AND FUTURE OF GOLD LOANS

To compete with NBFCs, banks have recently improved/streamlined their loan processes with some banks purchasing assaying machines to disburse loans in 15 minutes. This poses a challenge to the growing

dominance of NBFCs in the gold loan market, more so since banks usually charge lower rates of interest compared with NBFCs. The government considers gold loans as an effective means of meeting the demand for micro-finance in India. This would encourage framing of policies favourable to the growth of the gold loan market. Gold saving schemes have also emerged wherein the customers pay regular cash flows which on maturity are added with a certain amount of interest payment to purchase gold for customers. With frequent hikes in interest rates by the RBI and the subsequent hike in rates by banks, the cost of personal loan borrowing is increasing. This will lead to an increased consumer willingness to secure gold loans. Since more than 75% of the gold loan market is still with the unorganized segment as of 2010, the organized segment has a huge potential for growth through larger penetration, extensive networks and more efficient branches. The existing size of the gold loan market is approximately 1.2% of the total gold stock available. Hence there is a significant scope for further growth of the gold loan lending sector. India is one of the largest markets for gold accounting for ~10% (18,000- 20,000 tons) of the global gold stock. Rural India is estimated to hold around 65% of this. Shaped by sentimental and structural factors, country's demand for gold has been buoyant defying the phenomenal rally in price. It is estimated that ~10% of country's gold stock has been pledged, of which, ~75% is in the unorganized market (money lenders, pawn brokers, etc) and balance ~25% in organized market

CONCLUSION

For borrowers, gold loans have emerged as one of the best means of raising quick, short-term capital. For lenders, gold loans are more advantageous compared with home and car loans because of the shorter tenures, lower processing time and cost, and greater returns due to higher interest rates. These factors, along with appreciation in value of gold, have led to an explosion in the gold loan market. The organized sector is challenging the large unorganized gold loan market dominated by pawnbrokers and moneylenders, with NBFCs leading the pack due to simpler approval and disbursement processes, flexible products and better accessibility. Further expansion in the organized sector is required. When expanding, firms need to ensure consonance of services and operations throughout the network. Also efficient tracking of borrower accounts, process transparency and minimization of operational costs are essential. Firms need to manage risks related to possible sharp fall in gold prices and non-adherence of regulatory norms and also need to ensure that physical assets are properly valued, stored and documented. Firms need to invest in technology to better manage the increasing volumes and to reduce risks. Provision of accurate real-time information will lead to faster decision making and reduced turnaround time for loan disbursements.

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