Gold Prices and Demand in FY21

April 6th, 2021

Gold price movement

International gold prices (daily average) surged 24.7% YoY in FY21, higher than the 16% YoY growth in FY20. The primary reason for this surge during FY21 was the sudden outbreak of Covid-19 across the globe.

In January 2020, when the pandemic was announced a public health emergency, the international gold prices jumped 5.2% (Dec-19 to Jan-20). With each passing day, as more number of individuals were tested positive for the virus, most governments in the developed as well as developing nations imposed strict country-wide lockdowns, which created negative sentiments. This led to a rise in preference for investments in safe haven asset classes like the precious metals, by withdrawing funds from riskier alternatives like stock indices. Following which, a new rally in gold prices began. In the 1st week of August 2020, a fresh record was made when prices crossed $2,000/ounce for the first time in history. It continued in the same range for the successive few days and rose higher to touch $2,100/ounce, post which it stabilized and later started correcting.

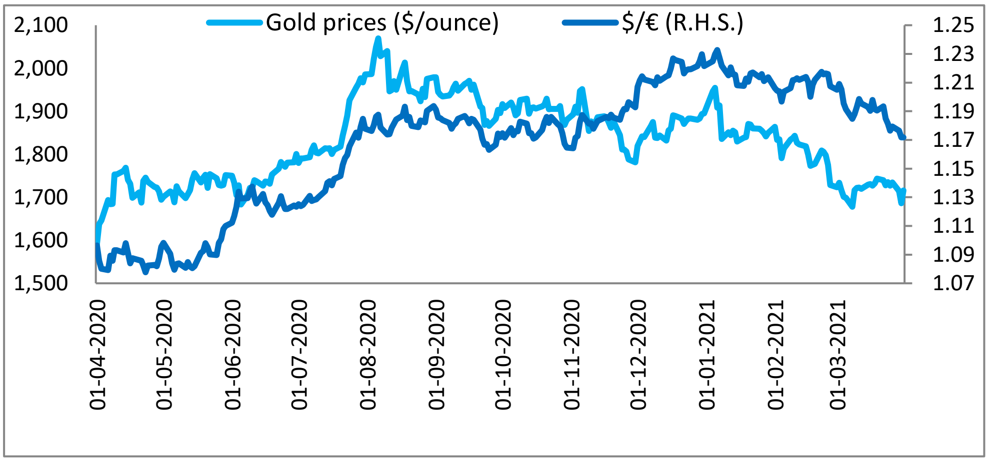
Did USD affect gold price movement?

A stronger USD generally tends to keep the international gold prices lower. This is because as the USD strengthens, gold gets costlier in other global currencies and with upward movement in price of any commodity, demand usually tends to recede. However, this relation did not hold true in all months of FY21, which means there were other factors at play that affected the gold price movement.

In April 2020, the USD/EUR rate averaged 1.09 while gold was around $ 1,700/ounce. By August 2020, the USD weakened to 1.18/EUR and gold rose to $1,980, which shows the regular inverse relation. The USD weakening can be attributed to the rising global uncertainties and hence announcements of various stimulus packages. However, in December 2020, there was a direct relation between the two variables, as the USD depreciated further to 1.22/EUR, but gold simultaneously fell to $1,864/ounce, which depicts the direct relation. By this time, gold lost its shine as lockdown restrictions were eased, better economic data flowed, interest yields rose and vaccine rollouts started.

The table below shows that the annualised daily volatility of USD/EUR stood at 6.5%, while it was nearly three times higher for gold at 18.8%. It can be concluded that when the degree of uncertainty in macro-economic environment rises, gold becomes a favoured investment, which is what the case was not only in FY21, but also in the prior year of FY20 which was witnessing some signs of slowdown and the start of a global recession.

Chart 1: Movement of international gold prices ($/ounce) and $/€



Volatility in FY21		
	$/€	Gold
Annual	6.5%	18.8%
Apr to Aug	6.9%	20%
Sept to March	6%	17.6%
Source: CARE Ratings		

Other factors at play

Other than the outbreak of covid-19 and USD volatility, multiple macro-economic variables affected the prices and demand of this precious metal in FY21, some of which are as follows:

- Supply:
  The fall in mine production and recycled gold contributed to the overall decline in gold supply of 15% YoY to 1,034 tonnes during Q1-FY21, as both were impacted by the response to the virus outbreak. While most industries were affected by the spread of the virus and mining being no exception, the gold mine production fell 10% YoY to 777 tonnes. The recycled gold simultaneously declined 8% YoY to 286 tonnes.

- Demand from large markets:
  China and India contribute ~60% of the global gold jewelry demand. The rising gold prices and various lockdowns led to a contraction in gold jewelry demand by 42% YoY for India and 24% YoY for China in 9M-FY21. With this, the global gold jewelry demand fell 31% YoY during the same period.

- Investment demand:
  H1-FY21 witnessed a strong demand for gold-backed Exchange Traded Funds (ETFs) and added 708 tonnes – which is more than double compared with similar period last year of 334 tonnes. However, in H2-FY21, net inflows in gold-backed ETFs declined by 201 tonnes. Demand for bars and coins as investment avenues rose by 16% YoY in 9M-FY21.

- Scrap sales:
  Due to the lockdown, large markets such as India did not witness high sales of scrap gold, as jewelry retailers has temporarily shut their stores during lockdowns. However, the situation improved after the lockdown restrictions eased. The rise in scrap sales built pressure on prices.

- Interest Rates
  While various government announced economic packages to support their nation's economies, interest rates were kept on the lower side. Gold prices, being inversely related to interest rates, saw a pick in gold demand and hence this contributed to escalation in its prices.

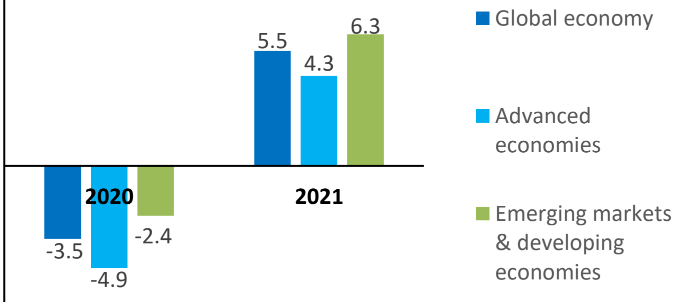
- Geopolitical tensions:
  For over three years now, political tensions between US and China have not shown any signs of reaching common grounds. The tensions gained further pace after the outbreak of Covid-19 and disrupted global trade not just between these two nations, but also between other countries that deal with US and China. Such uncertainties affecting business environment and contributed to investors preference for investments in safe haven assets.

- US elections:
  The US elections were an impactful event held in FY21. Mr. Biden's win created positive sentiments and led to a correction in gold prices.

- Vaccines:
  The successful trials and rollout of vaccines further added to the positive sentiments and made way for a faster recovery of global economy.

- Fears of economic slowdown and risk of recession:
  All macro-economic uncertainties cited above acted as speed-breakers for growth of the global economy in CY2020. According to IMF estimates released in April

Chart 2: Growth projections (%)



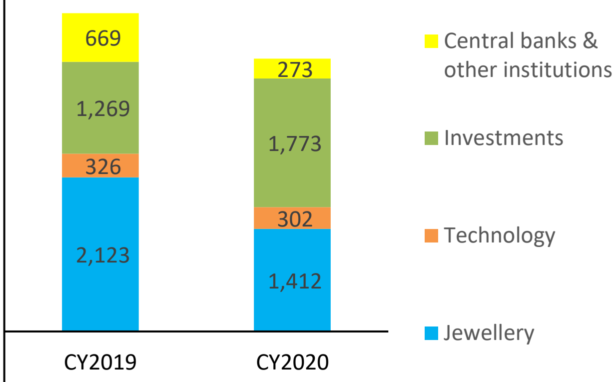
Source: Projections by IMF released in Jan 2021

2020, global economy growth in CY2020 was expected to decline 3%, much worse than that of 2008-09 financial crisis, while advanced economies were witness a higher decline of 6.1%. After several revisions, according to the new projections, as of January 2021, estimates the global economy to decline by 3.5% and advanced economies to decline by 4.9%. Such negative new flows affected the gold prices and its demand.

World gold demand

According to the World Gold Council, global gold demand in CY2020 declined 14% YoY to 3,760 tonnes, owing to a sharp fall from jewelry (-34% YoY) and central banks (-59% YoY). However, the investments in gold bars and coins rose 3% YoY and ETFs saw a rise of 120% YoY.

Chart 3: World gold demand



Source: World Gold Council

Concluding remarks

- In times of uncertainties like that of FY21, investors choose between multiple investment alternatives such as bonds, stocks, currencies and gold. While US 10-year Treasuries remained on the lower side in most part of the year, stock markets saw a sharp correction in the start but regained pace as economic data releases came in positive. The investments in bitcoin as an emerging asset class, gained pace especially towards the end of the year, mainly triggered by investment announcements made by a large US-headquartered automotive company. All macro-economic uncertainties created worries in minds of investors and gold gained favour in investors' portfolios. With an increasing demand, international prices of this precious metal jumped 24.7% in past 12 months. Domestic prices also gained new heights, but saw some correction in last two months of the year, as import duties were cut in the Union Budget.

Chart 4: Movement in stock indices

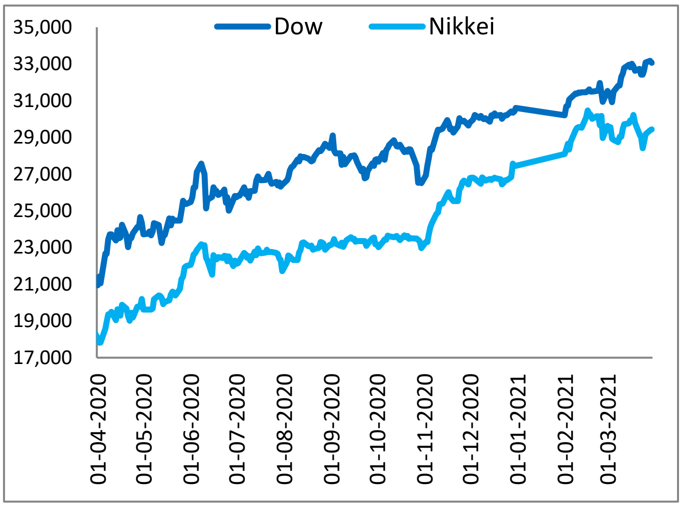
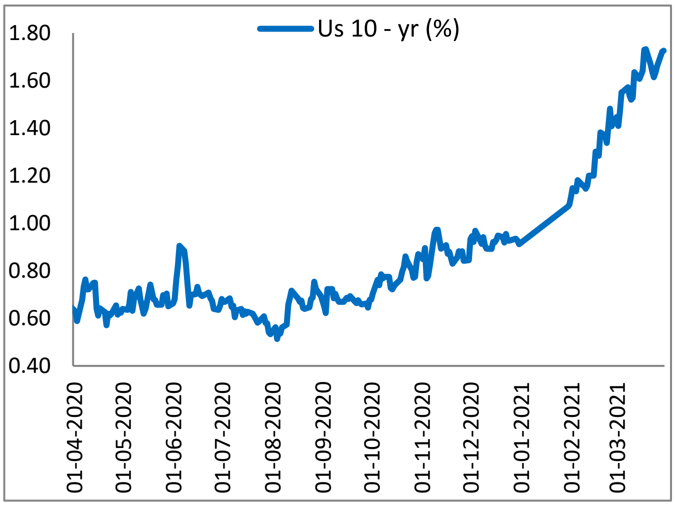


Chart 5: Interest rate



Outlook

- After a fall in the number of covid-19 cases by January 2021, it upended by March 2021 and most developed nations re-imposed strict lockdowns. This could trigger the large economies to announce further stimulus in following months, which may weaken the USD and help gain gold price the momentum which it lost in the end of CY2020. Additionally, the expectations of higher inflation, could be a positive for gold buying.

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