A STUDY OF INVESTOR'S PREFERENCE AND RISK & RETURN ANALYSIS OF PRECIOUS METALS (GOLD AND SILVER IN INDIA)

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Abstract: *Trading in commodities, in both cash and derivatives markets, as an alternative investment class to traditional portfolios comprising stocks and bonds, has grown significantly over the last decade. This reflects their use both as individual investments and as part of the diversified portfolios of hedge and other investment funds. The recent bull market of gold and other precious metal industry point to obvious questions: Are corporations' hedging strategies still valuable for their shareholders and how is this information reflected in the financial analysts' forecast? The impact of using derivatives on a firm's equity return is an ongoing issue in both corporate and asset management. Although theoretical literature describes why firms should or should not hedge, we do not know much about the empirical validity of these predictions. For our research purpose we have used various statistical tools to identify perceived risk and return of the investing in gold and silver.*

Key words: *Gold, Silver, Investor's preference, investments, Risk, Return*

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REVIEW OF LITERATURE

James Ross McCown on July 24, 2006 has carried out research on the topic, "Is Gold a Zero-Beta Asset? Analysis of the Investment Potential of Precious Metals" is,

Gold shows the characteristics of a zero-beta asset. It has approximately the same mean return as a Treasury Bill and bears no market risk. Silver also bears no market risk but has returns inferior to Treasury Bills. Both gold and silver show evidence of inflation-hedging ability, with the case being much stronger for gold. The prices of both metals are co - integrated with consumer prices, showing additional evidence of hedging ability.

James Ross McCown on July 23, 2007 has carried out research on the topic, "Analysis of the Investment Potential and Inflation-Hedging Ability of Precious Metals"

Gold and silver show strong evidence of ability to hedge stock portfolios and inflation during the period from 1970 to 2006. However, negative betas are only observed for the 1970s, suggesting that it is the inflation-hedging ability that is the cause of the stock hedging ability. Both metals show high correlation with expected future inflation as measured by the TIPS spreads, confirming Greenspans (1993) conjecture that gold prices are an indicator of expected inflation.

Jonathan A. Batten, Cetin Ciner and Brian M. Lucey on 1st June 2008, on the topic: "The Macroeconomic Determinants of Volatility in Precious Metals Markets" investigates that;

Key macroeconomic factors that impact the price returns of precious metals markets. The markets investigated were gold, silver, platinum and palladium; whereas the macroeconomic factors accommodated business cycle, monetary environment and financial market sentiment factors. The key findings present limited evidence that the same macroeconomic factors jointly influence the volatility processes of the precious metal price series, although there is some evidence of volatility feedback between the precious metals. This finding lends weight to views that individual commodities are too distinct to be considered a single asset class or represented by a single index; a finding of considerable importance for portfolio managers and investors.

Jung Ha Jun on May 2, 2009 has carried out research on the topic; "Global financial Crisis and Gold Market":

While most researches on the gold market have been focusing on empirical studies, few researches existed about how each macroeconomic phenomenon can affect gold market.

Gold is rarely dealt with macroeconomic perspective, because of lack of analyzing tools. However in this research, by including gold in a portfolio of risky assets and analyzing the portfolio indirectly, we can perform macroeconomic research on gold market. Specifically in this report, I focused on macroeconomic phenomena related to the global financial crisis.

Cetin Ciner and Brian M. Lucey in June 2010 has carried out research on the topic, "The macroeconomic determinants of volatility in precious metals markets" that;

The monthly price volatilities of four precious metals (gold, silver, platinum and palladium prices) and investigates the macroeconomic determinants (business cycle, monetary environment and financial market sentiment) of these volatilities. Gold volatility is shown to be explained by monetary variables, but this is not true for silver. Overall, there is limited evidence that the same macroeconomic factors jointly influence the volatility processes of the four precious metal price series, although there is evidence of volatility feedback between the precious metals. These results are consistent with the view that precious metals are too distinct to be considered a single asset class, or represented by a single index. This finding is of importance for portfolio managers and investors.

India heart of gold Revival (10 Nov 2010)

The report provides an analysis of the history, recent developments and the revival of Indian demand during 2010.further the report analyses the unique attributes of the Indian Jewellery market as well as the strategic outlook for Indian gold demand over the next few decades.

Linking global money supply to gold and to future inflation (February, 2010)

Many investors are raising concerns that strategies put in place by central banks across the globe – including what is commonly referred to as *quantitative Easing* – to reactivate the world economy and steer it away from a depression will ultimately debase fiat currencies and result in inflation. In order to study the relationship that movements in the price of gold have to inflation, we focus on its roots: money supply and velocity of money. We find that positive growth in money supply can explain increments in the price of gold from 6 to 9 months in advance, on average. We find that money supply can have an effect on the price of gold. As the money supply increases, the gold price rises. In particular, a 1% change in money supply in the US, the European Union and United Kingdom, India, and Turkey tend to correlate to an increment in the price of gold by 0.9%, 0.5%, 0.7%, and 0.05%, respectively.

Our analysis suggests, firstly that gold is a leading indicator of velocity and therefore inflation.

The impact of inflation and deflation on the case for gold (2010)

Gold's properties as an asset and its likely performance relative to other assets in a variety of different economic scenarios. The ongoing uncertainty surrounding many aspects of the global economy makes it especially appropriate that a wide range of alternative scenarios be covered. We seek to test gold's resilience as an asset in the face of possible shocks including high inflation, financial crises and deflationary conditions and also seek to assess its proper place in a long-run investment portfolio under different economic conditions. Gold benefits in this analysis from the fact that it has a zero or negative correlation with other assets so its inclusion in the portfolio reduces the overall volatility. As gold is correlated with inflation it shows relatively lower volatility than other assets, which do not move in time with inflation, compared to an analysis undertaken in nominal terms.

PROBLEM STATEMENT

Gold and all precious metals may be used as a hedge against inflation, deflation or currency devaluation. The recent bull market of gold and other precious metal industry point to obvious questions: Are corporations' hedging strategies still valuable for their shareholders and how is this information reflected in the financial analysts' forecast? The impact of using derivatives on a firm's equity return is an ongoing issue in both corporate and asset management. Although theoretical literature describes why firms should or should not hedge, we do not know much about the empirical validity of these predictions.

RATIONALE / NEED FOR THE STUDY

Investors are well aware of many of the reasons for having gold as part of their portfolio. Lately, these reasons have swirled around macroeconomic concerns. Traditions arose centuries ago in India of accumulating gold, using it for jewelry and other ornaments, and giving it as gifts for special occasions such as weddings. These traditions have continued to today, particularly in the rural regions of India. So it should come as no surprise that India is the world's largest consumers of gold. According to the World Gold Council, India consumed 963 metric tons of gold in 2010, and consumption is expected to exceed 1,000 metric tons this year. Traditionally, the country always bought gold in seasonal patterns. These patterns normally followed the festival calendar, with Akshaya Tritiya in May and the festival of lights, Diwali, in September, being peak buying periods. Also, the traditional wedding season, which runs from September to December, led to increased buying. So in the past, gold has been a cluster market in the summer, due to this lack of demand from the world's biggest consumer of bullion. However this summer, the scale of buying of precious metals from India has shocked traders. This estimate may be conservative, however, due to a change occurring in India that has gone little noticed by most American investors. As stock market globally fall down, investors again look in to gold market as the prices of gold are Quiet high and a measurement of an investment.

Top Reasons for investing in Gold and Silver

1) *Wealth Protection* – investing in Gold and Silver offers wealth protection against the ravages of inflation and consequent loss of purchasing power.
2) *Capital appreciation* – As demand increases and supplies continues to dwindle it will increase the value of both Gold and Silver. Gold has averaged over 17% return for the last nine years.
3) *Transferability* – It easy to sell Gold and Silver in its many forms and there is always a market for the precious metals.
4) *The ultimate diversification tool* **-** One thing about precious metals is that they provide the best way to diversify your portfolio.
5) *Central Banks policies* – With continued money printing by central banks around the world, purchasing power of paper currency is sure to erode.
6) *Fiscal Irresponsibility* – The United State budget deficit will approximate $ 1.5 dollars in the current fiscal year and there does not seem that it will decrease in the near future. Deficits are projected to stay above $1 trillion over the next ten years.
7) *Unfunded Government Liabilities* – Some estimate that when you include Medicare, Medicaid and social security the unfunded liabilities of the U.S government are in excess of $100 trillion.
8) *Low return of other assets* – Bonds yields are at all time lows, Certificate of Deposits are paying minuscule interest and the stock market has had a negative return for the last ten years when adjusted for inflation. Additionally these paper assets have higher inherent risk than owning physical gold and Silver.

9) *Purchases of gold by governments* – China and India have recently doubled their positions in gold and other governments have been accumulating as well.

10) *Flexibility in ownership* – There are many ways to own gold and silver including jewelry, bullion, ETF's and other methods.

11) *Privacy* – Depending on the way you own Gold it can be private and away from prying eyes.

OBJECTIVES OF RESEARCH

The purpose of research is to discover answers to questions through the application of scientific procedures. The main aim of research is to find out the truth which is hidden and which has not been discovered as yet. Though each research study has its own specific purpose, we may think of research objectives as falling into a number of following broad groupings:

1. To study different price drivers affect the Gold and silver.
2. To portray accurately the characteristics of a particular individual, situation or a Group (studies with this object in view are known as *descriptive* research studies)
3. To find out how price of Gold and silver fluctuate in Indian Commodity Market.

In view of objectives of the study and Literature reviews following Hypothesis have been developed:

RESEARCH METHODOLOGY

Research: 1 [Primary Research]

1. Type of Research: Descriptive
2. Scope of Research: Investors' preference for Gold and Silver in Ahmedabad city
3. Data collection method: Questionnaire
4. Data collection instruments: Hypothesis

Research: 2 [Secondary Research]

1. Target Population: Commodity Exchanges
2. Sampling Unit: Gold commodity traded on MCX Silver commodity traded on MCX
3. Sampling Techniques: Convenience sampling techniques
4. Sample Size: Prices of Gold and Silver listed on exchanges from years 2004 to 2011

FINDINGS

In our study we found that Gold and Silver are the most popular metals in India. Investors do invest in Gold and Silver with their other investment alternatives like stocks, mutual funds, real estate property etc. Another findings from the research is that before the year 2006, investors regularly make investment in Gold and Silver but they reduce their investment in such metals as the prices of Gold and Silver are at hike peak for the year 2007 and they have choose other options from the investment.

In Silver, coins of silver are most popular among the investors. For giving gifts to the relatives or friends. For giving bonus or appreciation on gift to the employees of the organization on special days. From our study of the investors' preference on investment in Gold and Silver by conducting research through questionnaire, we came to know that investors do invest in gold and silver depend on their income and savings with them.

Investors invest in gold and silver with the different purposes and the findings of the study state that more favorable purpose to invest in Gold and Silver is that it is more secure and can be utilize after long time also with beneficiary returns and the second major reason is that today there is volatility in the stock market and it is better to hedge risk by investment in precious metals like Gold and Silver.

Investors also believe that investment in Gold and Silver is the best investment option as it diversify the risk of the investment in other alternatives like stocks, mutual funds etc.

From the secondary research of our study we find that price of Gold and Silver were fluctuating for the period of 2004 to 2006, after that the prices of Gold and Silver shows booming trend from the year 2007. And till today the prices of Gold and Silver are showing bullish trend in the market.

The major reason behind the booming prices of Gold and Silver is the falling of US economy and inflation rate is higher in the market. So the stock market shows downward trend and prices of the stocks of the major companies' fell down. But commodities prices were not affected that much in the market and investors had started investing in commodity market and the demand of Gold and Silver were increased and till it is increasing. Investors now diversify their portfolio with different alternatives of the investment and mitigate the risk by their making diversification in the investment options.

Despite this factors, Gold and Silver are in demand in the market as they are not only the commodities but also they are used in various way like for making jewellery, use as gifts to friends and relatives and also organization gives bonus in the form of coins of Gold and Silver.

As finding of Exponential Moving Average of the Holding period returns of the Gold and Silver from 2004 to 2011, the trend shows that as Gold and Silver market going up today and if the scenario of the inflation and all the other commodities prices will increase, the Gold and Silver price will also increase. From our study of Investors' preference for investment in Gold and Silver, some investors are there, who do not invest in Gold and Silver rather they invest in Stock market, mutual funds, Properties etc.

The reasons they give that they are interested in getting returns from short term investment and they believe that investment in gold is of long term purpose. Some investors do not invest in Gold and Silver because the prices of gold and silver are very high in nature and also their income affects to their investment options. But if their income will increase in the future they will prefer to invest in Gold and Silver. precious metals were the best performing assets for the second consecutive year and also for the fourth time in the last five years. Investors enjoyed a 42% return by investing in precious metals in 2010.

One of the main reasons investors prefer investing in Gold and Silver is the stability witnessed in the market. Liquefaction is also an easy process for gold or silver bars and coins.

CONCLUSION AND SUGGESTION

Of all the precious metals, gold is the most popular as an investment. Investors generally buy gold as a hedge or harbor against economic, political or social fiat currency crises (including investment market declines, burgeoning national debt, currency failure, inflation, war and social unrest). Gold has been selected as an investment options in form of coins, bars, Exchange-traded Fund, gold certificates, derivatives and Mining companies. With the high risks associated with investments in share markets, large numbers of small investors have checked out from the share market and equity mutual funds into safer low risk high return assets like gold and land. Moreover, for the first time, Indians have converted proportionately more gold into investment than into jewellery. The change has been catalyzed by the rapid expansion of non-banking finance companies (NBFCs) into every

Indian city to allow the middle class to use gold as collateral for almost any type of investment From our study on investors' preference and risk and return analysis of precious metals specifically Gold and Silver, we come to the conclusion that many factors affect for making investment in Gold and Silver.

LIMITATIONS OF THE STUDY

Time constraint was one of the main limitations of the study. Also most of the information is collected from secondary data, so researcher can't say it 100% applicable. Cost Constraint - As the prices of Gold and Silver are very increasing in nature it is difficult for the investors to invest in that. Moreover, sometimes investors are not ready to give their details regarding investment in various options.

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