

# Commodities Market in Both Cash and Derivatives in Retail Exchange – A Review

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## Abstract

This paper looks at trading in commodities retail sector like gold and silver, in both cash and derivatives markets, as an alternative investment class to traditional portfolios targeting investors attitude to it. 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. Investing money silver and gold as commodity is simple and profitable. Anyone can learn the easy ways of buying silver and gold as a physical wealth. Since the value of gold and silver is considerably high, the precious metal constitutes to be great investment option.

Investing in gold and silver has more advantages as compared to any form of currency. While people give a lot of opinions, investing in gold has always come out as a clear winner. It was noted after US' 2008 debt crisis, the world bought both gold and silver in bulk. This resulted in dramatic increase in the price of silver and gold between from 2008 to 2013. At that time price of silver went up to nearly Dollars 45 per ounce. Currently, the craze of silver bubble has fizzed out but gold still continues to shine. Apart from by the investors, silver is also considered a precious metal because of its application, including its use in industries like mobile hand-sets, glass, normal lead acid batteries, solar panels, electric conductors, computers and so on. It is a surprise to see that no other metal has been able to replace silver in this industry. Additionally, silver is used in many life saving medicines as well. Silver is known as a poor man's gold, because comparatively gold, which is traded at 1400 dollars per ounce, silver trades at just 25 dollars per ounce. Investors or nations buy Gold for accumulation only, but silver has many other industrial applications apart from investment. But, if we compare gold and silver investment, then silver is considered to be a lot more useful metal than gold. Each and every ounce of gold that is mined out has either been stored in the world's central bank or in the lockers of people. Price of gold has always trades at exorbitant prices because of the huge imbalance in its demand and supply. The global trend and brand name of gold also contribute in its unreasonably high pricing.

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

## Introduction

Gold is unique for its durability (it doesn't rust or corrode), malleability, and its ability to conduct both heat and electricity. It has some industrial applications in dentistry and electronics, but we know it principally as a base for jewelry and as a form of currency.

The value of gold is determined by the market 24 hours a day, seven days a week. Gold trades predominantly as a function of sentiment—its price is less affected by the laws of supply and demand. This is because new mine supply is vastly outweighed by the sheer size of above-ground, hoarded gold. To put it simply, when hoarders feel like selling, the price drops. When they want to buy, new supply is quickly absorbed and the gold prices are driven higher.

Even the petty investors can go ahead and invest in silver easily. Gold and silver have been recognized as valuable metals, and have been coveted for a long time. Even today, precious metals have their place in a savvy investor's portfolio. But which precious metal is best for investment purposes? And why are they so volatile?. There are many ways to buy into precious metals like gold, silver, and platinum, and a host of good reasons why you should give in to the treasure hunt. Unlike gold, the price of silver swings between its perceived role as a store of value and its role as an industrial metal. For this reason, price fluctuations in the silver market are more volatile than gold. But comparatively, in terms of gold vs silver investment it is noted that that silver is still traded at a much economical price.

So, while silver will trade roughly in line with gold as an item to be hoarded (investment demand), the industrial supply/demand equation for the metal exerts an equally strong influence on its price.

## Objective:

This paper intends to deal with investment and business opportunities offered by silver, gold and other precious metals. With attention given to investor sentiment and attitude

## Positive attitude towards gold in India

The place of gold in the hearts, minds, jewellery boxes and investment portfolios of Indians is a constant. But the relationship we share with this most precious element is constantly evolving. Gold has always been a reliable store of value that works as a hedge against inflation to secure the financial future of our loved ones. Gold today has gone digital with newer avenues of investment opening up beyond its physical forms like bars, coins and jewellery. However, Indians trust that gold's ownership demands respect and hence believe in buying and gifting gold jewellery, bars and coins on special occasions.

## 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

Investment is the deployment of fund with the aim of achieving additional income or growth in capital value. Investment is an investing activity that attracts all people irrespective of their occupation, education and social status. An understating of the core concepts and a thorough analysis of the options can help investors to create a portfolio that maximize returns while minimizing risk exposure. The general concern and focus of the financial advisors and government is to see that every individual needs to invest and earn returns on their idle resources and generate a specified sum of money for a specific goal in life and make a provision for an uncertain future. The financial investment is the obligation of money that is expected to yield some gain over a period of time. If a person has more funds than his current needs he can deposit the surplus money in the bank to earn a fixed rate of interest or buy gold or purchase shares or invest in any other form of financial instruments. In other words, investment is allocating of monetary resources to assets that are expected to yield some gain or positive return over a period of time. The assets may range from safe investment to risky investment. 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. 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.

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.

Here's a look at the positive attitudes older and newer generations have towards gold:

### **How gold has been viewed across Indian families?**

- Growing up, Indians have noticed their grandparents and parents collecting gold coins. They did so because owning gold has always instilled a sense of safety and security about the future in their minds. Inherently, young Indians too are inspired by them and view gold as a default way of saving and investing in a secure future.
- In Indian culture, gold is also known to drive good luck and fortune and hence is bought for all important life events.

### **How gold is an important, reliable investment?**

- Gold is known as a solid and stable means to protect wealth as it known to help people achieve their lifelong goals and ambitions.
- Its tangibility brings a sense of security and credibility to its owner.
- People have positive attitudes when it comes to owning gold.
- 72% of Indians believe that gold will never lose its value over the long-term.
- 63% Indians trust gold more than the Indian currency as it provides a hedge against inflation and economic turbulence.
- 70% of Indians said that owning gold made them feel secure.
- Indians are optimistic about future gold prices and hence consider it a reliable investment avenue.

### **Upcoming trends in gold investment**

- Investors acknowledge gold's robustness and ability to retain its value over the long-term
- Indians want to invest more in gold, regardless of their income
- Investing 24%-30% of his/her income over an average of 3.8 products, the urban Indian is young, enthusiastic and speculative

The positive outlook that Indians have towards gold suggests huge untapped potential among investors, especially given the many modern ways of investing in gold- from ETFs to gold jewellery purchase scheme to gold being sold via Mobile app-based payment and mobile wallet services such as PhonePe and Paytm.

## Filling Up Treasure Chest

Let's take a look at the options available to those who want to invest in precious metals.

1. **Commodity ETFs:** Exchange traded funds exist for all three precious metals. ETFs are a convenient and liquid means of purchasing and selling gold, silver or platinum. Investing in ETFs, though, doesn't give you access to the physical commodity, so you don't have a claim on the metal in the fund. You will not get actual delivery of a gold bar or silver coin.
  2. **Common stocks and mutual funds:** Shares of precious metals miners are leveraged to price movements in the precious metals. Unless you're aware of how mining stocks are valued, it may be wiser to stick to funds with managers with solid performance records.
  3. **Futures and options:** The futures and options markets offer liquidity and leverage to investors who want to make big bets on metals. The greatest potential profits and losses can be had with derivative products.
  4. **Bullion:** Coins and bars are strictly for those who have a place to put them like a safety deposit box or safe. Certainly, for those who are expecting the worst, bullion is the only option, but for investors with a time horizon, bullion is illiquid and downright bothersome to hold.
1. **Certificates:** Certificates offer investors all the benefits of physical gold ownership without the hassle of transportation and storage. That said, if you're looking for insurance in a real disaster, certificates are just paper. Don't expect anyone to take them in exchange for anything of value.

## Will Precious Metals Shine ?

Precious metals offer unique inflationary protection—they have [intrinsic value](#), they carry no credit risk, and they cannot be inflated. That means you can't print more of them. They also offer genuine "upheaval insurance" against financial or political/military upheavals.

From an investment theory standpoint, precious metals also provide low or negative correlation to other asset classes like stocks and bonds. This means even a small percentage of precious metals in a portfolio will reduce both volatility and risk. The main problem related to this real commodity is the issue of “the undervaluation” of its investment options, if compared to gold. If considering silver as the investment option, its investment potential is significantly enhanced by its industrial usage. The aim of this paper is to highlight business and investment opportunities for both professionals and non professional investors at the commodity markets. The price growth of this investment and industrial metal can generate profits for the investors. And on the other hand, industries which cannot do without silver in their production may efficiently utilize the knowledge of setting up its price at the markets.

## Precious Metals Risks

Every investment comes with its own set of risks. Although they may come with a certain degree of security, there is always some risk that comes with investing in precious metals. Prices for metals can drop during times of economic certainty, putting a damper for people who like to invest heavily in the precious metals market. Selling may be a challenge during times of economic volatility, as prices tend to shoot up. Finding a buyer for physical metals may be difficult.

Another risk to precious metals prices includes the issue of supply. When demand shoots up, the existing supply may begin to deplete. And that means producers will have to bring more of each metal into the market. If there is a short supply of mineable metals, that could put pressure on prices. Commodity markets distinguish two large groups of traded raw materials.

The first one consists of renewable commodities, represented by agricultural products especially: wheat, corn, coffee, soybeans. The second group includes non-renewable resources, represented by oil, energy, aluminum and silver. Some metals of the non-renewable resources, silver included, are used for the investment and for the production in industries. Regardless of the market, the investor decides for, current conditions set up for individuals and businesses are generally the major aspects for investments. These may be supportive or discouraging; defined by the business environment, government, and current legislation. Purchasing power of investors and their willingness to invest accumulated funds in order to get gains indicate the transparency level of the investment environment within the current legislation context. If you invest a sizeable part of your capital in physical bullion, you might not want to keep your metal at home (you'll need a safe and perhaps other additional equipment). In this case, you might prefer to choose a custodian – an institution that stores your metal for you. This storage service is not free of charge (neither is transportation to the storage facility, nor its insurance), so you need to take this cost into account, and it diminishes your returns on gold. By buying paper gold, you get a paper that more or less reflects the price of gold and allows you to avoid the cost and headache of storage.

In addition, paper gold enables you to invest in gold even if you don't have enough capital to buy an ounce of gold. This is because ETF shares, or similar investment vehicles, usually reflect less than one ounce of gold – most commonly they follow the price of 1/10 of an ounce. If you do not have enough money to buy a full ounce, ETFs might be a solution. This is another reason for the popularity of ETF vehicle with individual investors.

## **Conclusion**

Precious metals provide a useful and effective means of diversifying a portfolio. The trick to achieving success with them is to know your goals and risk profile before jumping in. The volatility of precious metals can be harnessed to accumulate wealth. Left unchecked, it can also lead to ruin. 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

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