Capital League

PRIVATE WEALTH MANAGEMENT

Gold

A Strategic Asset for Stability and Diversification

Knowledge Series

Investment in Gold: A Strategic Asset for Stability and Diversification

Gold has held a unique place in human history: from ancient currency and cultural symbolism to today's reserve and investment asset. While it does not generate income like equities or bonds, gold offers diversification, liquidity, and a proven store of value during inflationary shocks, financial crises, and geopolitical instability. Investment in Gold is a time-tested strategy for mitigating portfolio risk, especially during economic uncertainty.

A Historical Perspective on Gold

source: goldprice.org

Ancient Times

Gold was central to the civilization in ancient times. It has been valued for 5,000+ years for its rarity, malleability, and resistance to corrosion. It functioned as money in Egypt, Rome, India, and China.

19th Century

The Classical Gold Standard (1870s–1914) linked major currencies to gold, stabilising exchange rates and anchoring trust in global trade.

Bretton Woods (1944–1971)

After World War II, the US dollar was convertible into gold at $35/oz. In 1971, the US ended this convertibility, and gold became a freely traded asset.

1970s inflation era

Gold rose nearly 20x (from ~$35/oz to >$600/oz) as inflation and oil shocks eroded fiat currency credibility.

2000s commodity boom

Gold rallied with rising demand from China/India and concerns about US deficits.

Global Financial Crisis (2008–09)

Gold rose ~21% in USD terms as global equities collapsed, proving its crisis-hedge role.

COVID-19 pandemic (2020)

Gold hit new highs above $2,050/oz amid monetary expansion and uncertainty.

Russia Ukraine crisis (Feb 2022 onwards)

Gold has risen sharply since the sanctions imposed on Russia after its invasion of Ukraine. Demand from central bankers rose for gold as a strategy of 'De- dollarisation'.

2025 context: Gold has moved up sharply, driven by increasing global uncertainty, inflation, currency volatility, central bank reserve demand, geopolitical risk, and de-dollarisation.

Key Benefits of Investing in Gold

Portfolio Diversification

Gold is considered to balance portfolios against the volatility of other asset classes, particularly during economic uncertainty.

Buffer against currency depreciation

Being a globally priced metal, it acts as a hedge against currency depreciation.

Buffer against geopolitical shocks

Gold has been perceived as a safe haven since ancient times. Investors generally turn towards gold when adverse geopolitical events occur.

Demand from Central Banks

Central Banks have increased gold purchases to diversify their Foreign Forex Reserve holdings which could potentially support the gold rally.

Mode of Investment in Gold:

Gold investment can be done as a physical asset or as a financial asset as in a mutual fund/ETF that replicates its spot price, or futures and options in commodities market or as a Sovereign gold bond scheme. Based on the investor’s choice, preference and convenience of investing an investor can choose any of the following modes of investment:

- **Physical Gold:**
  This is the conventional method of investment in gold as jewelry, coins, bars etc. While it offers emotional and cultural value, it comes with challenges related to purity, storage, and liquidity.

- **Gold Exchange Traded Funds (ETFs) / Mutual Funds:**
  This is a passive form of digital investment that tracks the domestic price of physical gold. Each unit of a Gold ETF usually represents one gram of 99.5% pure gold and is traded on stock exchanges. A demat and trading account is required to invest in Gold ETFs. Whereas in a gold MF investment can be made in a convenient way, even by way of SIP, without a demat or trading account. This mode of investment is risk free in terms of safety and security as there is no storage requirement.

- **Sovereign Gold Bonds:**
  These are the safest way to buy digital Gold as they are issued by the Reserve Bank of India on behalf of the Government of India with an assured interest of 2.5% per annum. The bonds are denominated in units of grams of gold with a basic unit of 1 gram. These bonds have a tenor of eight years with an exit option from the fifth year onwards. The investor will have the ownership of gold without any physical possession. Added advantage; no tax on capital gains if held till maturity.

Investment in physical gold vis-à-vis Digital Gold

Challenges of Physical Gold Ownership

- **Voluminous Nature:**
  Means they require substantial storage space.

- **Storage and Security Risks:**
  Holding physical gold or silver necessitates secure storage, which can involve costs (e.g., bank lockers) and carries inherent risks of theft or damage.

- **High Costs and Impurities:**
  When buying physical jewellery, investors often incur significant "making charges." Later, if the jewellery needs to be sold or converted, "breaking charges" might apply, and purity can be a concern.

Digital Gold Investment

- **Convenience & Safety:**
  Invest in physical gold and silver on your behalf, eliminating the hassle of physical storage, security concerns, and associated costs.

- **Assured Purity:**
  Backed by physical gold of high fineness (typically 99.5% or above for gold) and silver of high fineness (typically 99.9% or above for silver), complying with industry standards.

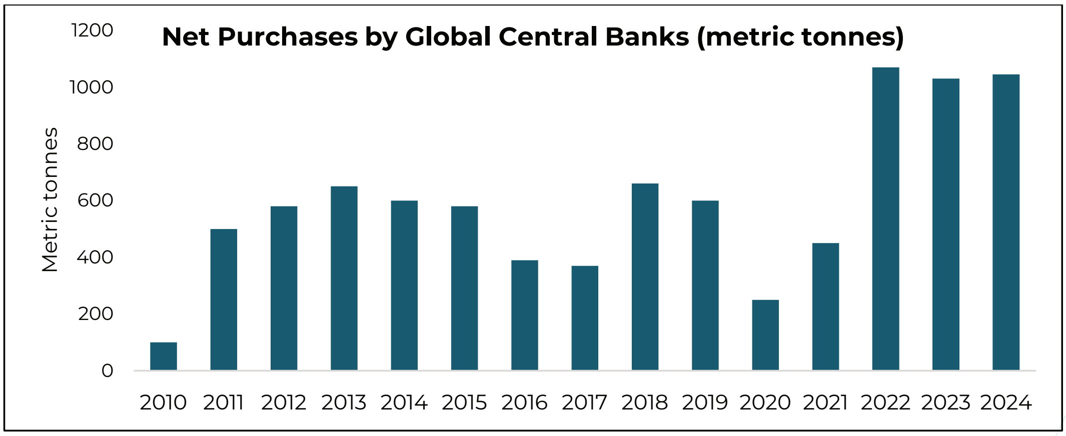
- **Liquidity:**
  ETFs are traded on stock exchanges. Mutual Funds allow investors to invest or redeem units directly with the Asset Management Company (AMC) on a daily basis, offering ease of transaction.

- **Lower Cost:**
  Ideal vehicle for long-term investment due to lower expense ratios

Why Gold Now:

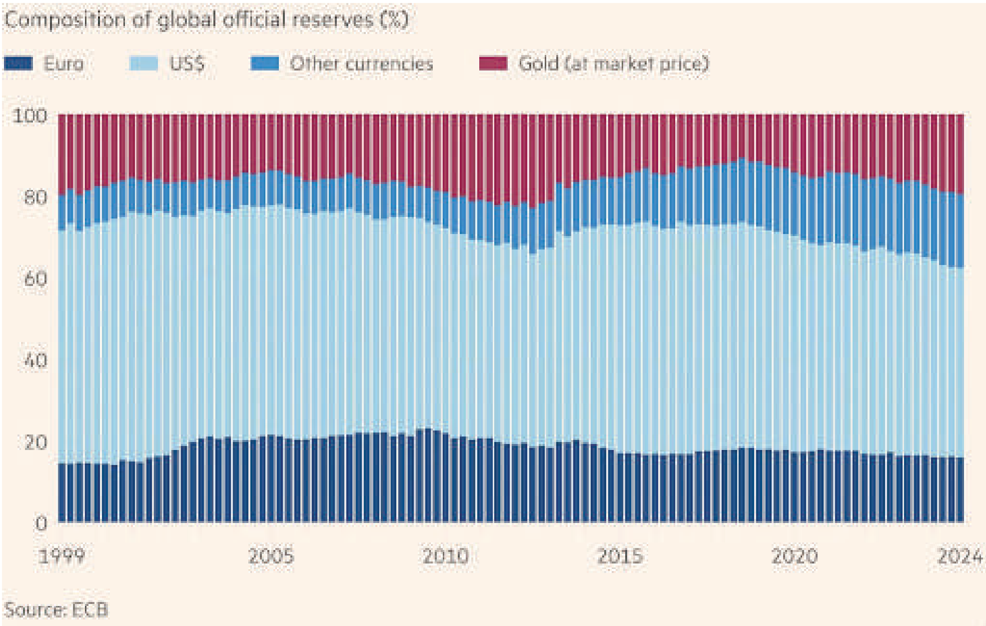
As of September 2025, gold has reached record highs above **$3,700/oz**, with Indian prices crossing **₹1.10 lakh per 10g**. This strength reflects a structural shift in global reserves (de-dollarisation), record central-bank buying, sticky geopolitical risks, and a macro environment that increasingly favours non-yielding hedges.

- **Central Bank demand:**
  Motivated by **de-dollarization**, inflation hedging and reducing exposure to USD. Central bankers are buying gold in record amounts.

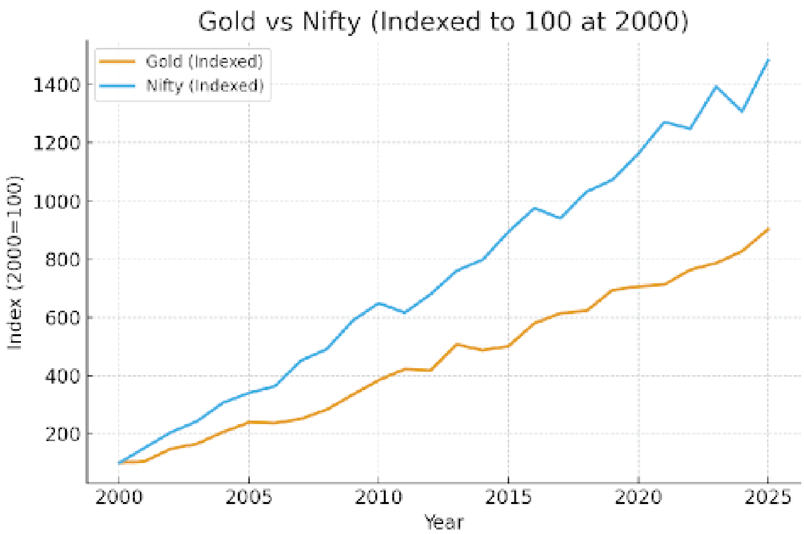


Since 2022, gold purchases have touched **~1,080–1,100 tonnes annually**. In **2025**, central banks purchased a **record 682 tonnes of gold in Q1 alone**, exceeding the pace of previous years. **Reserve bank of India** added a record **57.5 tonnes in FY25**, reaching total holdings of ~880 tonnes by March'25. The Emerging markets (China, India, Turkey, Middle East) diversifying away from US Treasuries.

- **Gold is the Second most important reserve asset, after USD:**
  Gold now represents **~20% of global reserve assets**, surpassing the euro, second only to the US dollar (~46%). As the Gold is the **only neutral, universally accepted reserve asset** not tied to any single country's credit risk. Many countries are **settling trade in local currencies or gold** to reduce USD exposure. This trend enhances the **strategic demand** for gold, making it more than just a cyclical play.



- **Gold is Outshining equities amid global uncertainty:**
  Gold has delivered standout performances in 2025, with gold prices rallying ~40% YTD. Gold has a negative correlation with equity as an asset class, hence act as an effective and reliable hedge against the stress in equity markets. Even when equity markets perform well, gold does not necessarily exert a significant drag on portfolio returns.



Source: NSE, MCX

- **Risks:**
  After strong rallies in Gold prices, corrections of 10–20% are common. Rising US real rates or dollar strength could cap upside. Gold's role is as a hedge, not a growth engine as historically equities deliver superior long-term compounding. Policy changes related to Import duties or taxation pose risk to investment in Gold.

Conclusion

Gold remains an essential component of a well-rounded investment strategy, offering:

- Diversification benefits through its low correlation with equities.
- A hedge against currency depreciation, geopolitical tensions, and market volatility.
- Stability as a safe-haven asset during uncertain times.

Allocation of 5–10% weight to gold in an asset allocation reduces volatility and improves risk adjusted returns ratio, even if gold's long-term CAGR is lower than equities. Investments done in a staggered manner or SIPs manages the volatility risk after sharp rallies.

Additionally, in India, with debt mutual funds taxation aligned with fixed deposits at the marginal tax rate of each investor, investment in gold funds offers an attractive tax arbitrage, potentially delivering superior post tax returns than fixed income assets.

With central bank demand, supportive interest rates, and de-dollarization trends, gold's role in portfolios is increasingly vital, offering a resilient and versatile investment to safeguard wealth.