5. Gold Import - economy

Recently, the Prime Minister of India urged citizens to postpone non-essential gold purchases and reduce petroleum consumption to conserve India's foreign exchange reserves with the West Asia crisis entering its third month.

1.Background

Gold occupies a unique position in Indian society and economy, deeply embedded in cultural traditions, religious ceremonies, and wealth preservation practices spanning millennia. India is one of the world's largest consumers of gold accounting for approximately 800 tonnes annually representing roughly 25-30% of global demand, driven by weddings, festivals, investment preferences, and jewellery traditions. However, domestic gold production is negligible with most demand met through imports making India the world's second-largest gold importer after China, creating significant balance of payments implications. Historically, India's gold imports have contributed substantially to current account deficit, particularly during periods of high international prices and strong domestic demand. The 2013 "taper tantrum" crisis when gold imports surged to over $50 billion widening current account deficit to 4.8% of GDP forced the government to impose import restrictions and raise duties highlighting gold's macroeconomic sensitivity.

Despite various policy interventions including higher import duties, gold monetization schemes, sovereign gold bonds, and gold exchange-traded funds aimed at reducing physical gold demand, imports have remained stubbornly high reflecting deep-rooted cultural preferences and limited trust in alternative financial instruments. Recent geopolitical developments have exacerbated the situation—the West Asia crisis entering its third month has created uncertainties about oil supplies and prices simultaneously affecting petroleum and gold imports, while global gold prices have surged over 40% driven by safe-haven demand amid geopolitical tensions, currency uncertainties, and inflation concerns. India's gold imports in FY26 rose sharply despite lower physical volumes because of steep increases in global gold prices—import value jumped nearly 25% to $71.97 billion even as physical quantities declined, demonstrating how commodity price shocks affect India's balance of payments independently of consumption changes.

The India-UAE Comprehensive Economic Partnership Agreement signed in February 2022 to strengthen bilateral trade and investment inadvertently created unintended consequences for gold imports. The agreement's tariff concessions inadvertently inverted the intended duty differential between bullion (refined gold) and doer (semi-pure gold alloy), making bullion imports relatively more attractive than doer imports, reducing opportunities for domestic refining and value addition. This structural issue combined with India's weak gold refining ecosystem despite being world's largest consumer means India remains largely an end consumer rather than value-added participant in global gold supply chains, missing opportunities that countries like Switzerland and UAE have leveraged to become major refining and trading hubs despite negligible domestic production.

2.Why Gold Imports Matter for India

India's Gold Consumption Pattern

1. India is one of the world's largest consumers of gold accounting for significant share of global demand.
2. However, domestic production is negligible, forcing the country to rely heavily on imports to meet demand.
3. Gold consumption is driven by weddings, festivals, religious ceremonies, investment purposes, and jewellery preferences.
4. Cultural traditions and wealth preservation practices make gold demand relatively price-inelastic.

Rising Gold Import Bill

1. India's gold imports in FY26 rose sharply despite lower physical volumes because of a steep increase in global gold prices.

2. Gold import value rose by nearly 25% in FY26 to $71.97 billion.
3. Physical imports declined, but prices surged by over 40% globally, inflating the import bill significantly.
4. It demonstrates how commodity price shocks can affect India's balance of payments even without a rise in consumption.

Macroeconomic Implications

1. Excessive gold imports become a macroeconomic challenge during periods of global uncertainty because they increase the Current Account Deficit, put pressure on foreign exchange reserves, depreciate the rupee, increase imported inflation, and worsen external sector vulnerability.
2. Gold constitutes major non-essential import item alongside petroleum, both of which significantly influence trade balance.

3.Impact on India's Economy

Pressure on Current Account Deficit

1. Gold constitutes a major non-essential import item that does not contribute to productive capacity.
2. Rising imports widen the trade deficit, especially when oil prices are simultaneously high.
3. A higher CAD increases dependence on foreign capital inflows to finance the deficit.
4. Sustained high CAD levels can trigger currency crises if foreign capital inflows reverse suddenly.

Stress on Forex Reserves

1. Higher import payments require larger outflows of dollars to settle international transactions.
2. It reduces the Reserve Bank of India's ability to stabilize the rupee during external shocks.
3. According to RBI data and government assessments, maintaining adequate forex reserves is crucial for import cover, exchange-rate stability, and investor confidence.
4. Reserves provide buffer against sudden capital outflows and external payment difficulties.

Rupee Depreciation

1. Large dollar demand for gold and crude oil imports weakens the rupee against major currencies.
2. A depreciated rupee further raises import costs, creating a vicious cycle of inflation.
3. Rupee depreciation makes all imports expensive including capital goods, technology, and essential inputs.
4. Currency volatility creates uncertainty for businesses engaged in international trade and investment.

Inflationary Pressures

1. Rising gold and oil prices increase imported inflation affecting overall price levels.
2. This complicates monetary policy management for the RBI which must balance growth and inflation objectives.
3. Higher inflation erodes purchasing power particularly affecting fixed-income households.
4. Inflation expectations can become entrenched requiring prolonged tight monetary policy.

4.India-UAE CEPA and Gold Imports

Agreement Background

1. India and the UAE signed the Comprehensive Economic Partnership Agreement in February 2022 to strengthen bilateral trade and investment.
2. The agreement aimed to boost bilateral trade, attract investment, and deepen economic integration.
3. However, some tariff concessions under the agreement unintentionally increased bullion imports.

Unintended Tariff Inversion

1. The agreement inadvertently inverted the intended duty differential between Bullion (refined gold) and Dore (semi-pure gold alloy).
2. As a result, India imports more finished gold instead of refining it domestically.
3. A working paper of IIM Ahmedabad highlighted that India imports large quantities of finished bullion rather than raw dore.

4. Tariff structure under CEPA made bullion imports relatively more attractive than dore imports.
5. It reduced opportunities for domestic refining and value addition missing potential revenue and employment.

Lost Value Addition Opportunities

1. Importing refined bullion instead of raw dore means India loses opportunities for domestic value addition.
2. Refining generates nearly 40% value addition which could offset trade deficits through exports.
3. Domestic refining industry remains underutilized despite significant installed capacity.
4. Employment opportunities in refining sector remain unrealized.

5.Weak Gold Refining Ecosystem

India's Refining Gap

1. Despite being one of the world's largest consumers of gold, India has not emerged as a major global gold refining and trading hub.
2. Countries such as Switzerland and the United Arab Emirates have developed strong refining ecosystems despite having negligible domestic gold production.
3. They developed world-class refining infrastructure, LBMA-accredited refineries, and integration with global supply chains.
4. Refining generates nearly 40% value addition, helping offset trade deficits through exports of refined gold.

Challenges For India

1. Lack of LBMA-Accredited Refineries - India currently lacks globally recognised LBMA-certified refineries, limiting access to international bullion markets.
2. London Bullion Market Association accreditation is gold standard for refineries enabling participation in global trade.
3. Without LBMA accreditation, Indian refineries cannot supply to major international markets.
4. Underutilised Capacity - Existing refineries operate below potential due to policy and structural issues including tariff distortions and regulatory uncertainties.
5. Limited Global Integration - India remains largely an end consumer rather than a value-added participant in global gold supply chains.
6. Import Structure Bias - The import ecosystem favours refined bullion imports over domestic processing due to tariff anomalies.

6.Government Measures and Policy Suggestions

Short-Term Measures

1. Demand Management - Discouraging non-essential gold purchases through public appeals and awareness campaigns, and encouraging financial savings instruments including mutual funds, stocks, and fixed deposits as alternatives to physical gold.
2. Import Controls - Historically, India has used higher import duties, gold monetisation schemes, and sovereign gold bonds to reduce physical gold demand.
3. Import duty increases make gold expensive reducing demand temporarily but face resistance from industry.
4. Gold monetization schemes encourage households to deposit idle gold earning interest but have had limited success.
5. Sovereign Gold Bonds offer returns linked to gold prices plus interest without physical possession but uptake remains modest.

Long-Term Structural Reforms

1. Develop Refining Ecosystem - Establish LBMA-accredited refineries meeting international standards, and encourage domestic value addition through incentives, infrastructure support, and streamlined regulations.

2. LBMA accreditation requires substantial investments in technology, quality control, and assaying capabilities.
3. Government support through capital subsidies, tax incentives, and regulatory facilitation can accelerate refinery development.
4. Promote Gold Recycling - India has significant idle household gold reserves estimated at over 25,000 tonnes.
5. Establishing formal recycling infrastructure can reduce import dependence while providing income to households.
6. Recycled gold can feed domestic refining operations reducing raw material import requirements.
7. Expand Financial Alternatives - Encourage SGBs, gold ETFs, and digital gold to reduce dependence on physical imports.
8. Financial gold products provide price exposure without import requirements when held electronically.
9. Better awareness and distribution can increase adoption particularly among younger generations.
10. Review CEPA Tariff Structure - Ensure trade agreements support domestic manufacturing and refining rather than inadvertently undermining them.
11. Duty differential should Favor dore imports over bullion imports incentivizing domestic refining.
12. Periodic reviews of trade agreements should identify and correct unintended consequences.
13. Strengthen External Sector Resilience - Diversify exports reducing dependence on few products and markets, reduce oil dependence through renewable energy and electric mobility, and improve forex management through hedging and reserve accumulation.

7.Way Forward

Balance Demand Management and Supply-Side Reforms

1. Short-term demand management measures including public appeals and import duties should be complemented by long-term supply-side reforms developing domestic refining ecosystem, promoting gold recycling infrastructure, and expanding financial gold alternatives reducing physical gold import dependence, while ensuring measures do not disrupt legitimate jewellery industry and employment.

Develop LBMA-Accredited Refining Infrastructure

1. Government should provide capital subsidies, tax incentives, and regulatory facilitation for establishing LBMA-accredited refineries meeting international standards, enabling India to import doer for domestic refining rather than finished bullion, generating nearly 40% value addition, creating employment, and potentially exporting refined gold offsetting import bills.

Promote Gold Monetization and Recycling

1. Strengthen gold monetization schemes encouraging households to deposit idle gold earning interest, while establishing formal recycling infrastructure with transparent pricing and quality assurance creating alternative supply reducing import requirements, and leveraging India's estimated 25,000 tonnes household gold reserves through innovative financial products.

Review and Correct Trade Agreement Anomalies

1. Conduct comprehensive review of India-UAE CEPA tariff structure identifying unintended inversions favouring bullion over doer imports, while ensuring duty differentials incentivize domestic refining and value addition, and establishing mechanisms for periodic trade agreement reviews preventing future unintended consequences affecting domestic industries.

Strengthen External Sector Fundamentals

1. Diversify export basket reducing dependence on few products and markets while expanding manufacturing exports, accelerate renewable energy adoption and electric vehicle transition reducing petroleum import dependence, improve forex reserve management through prudent

policies, and enhance trade competitiveness through infrastructure development, ease of doing business, and skill development supporting external sector sustainability.

Conclusion

India's gold import problem has intensified with FY26 imports rising nearly 25% to $71.97 billion despite lower physical volumes due to global prices surging over 40%, demonstrating commodity price shock impacts on balance of payments. Excessive gold imports create macroeconomic challenges including pressure on Current Account Deficit, stress on foreign exchange reserves, rupee depreciation, and inflationary pressures complicating RBI monetary policy management. India-UAE CEPA signed February 2022 inadvertently inverted duty differential between bullion and dore making finished gold imports relatively more attractive than raw material imports, reducing domestic refining opportunities. Despite being world's largest gold consumer, India lacks LBMA-accredited refineries, has underutilized refining capacity, limited global integration, and imported structure bias favouring bullion over dore. Addressing challenges requires balancing short-term demand management through public appeals and import controls with long-term structural reforms including developing LBMA-accredited refining infrastructure generating 40% value addition, promoting gold monetization and recycling leveraging 25,000 tonnes household reserves, reviewing CEPA tariff anomalies, and strengthening external sector fundamentals through export diversification and petroleum dependence reduction ensuring India transforms from end consumer to value-added participant in global gold supply chains.
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