Gold Economy of India

Gold Economy of India:

An In-Depth Study on Gold Demand and Associated Factors in India

By

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TABLE OF CONTENT

Chapter I 1
Introduction

Chapter II 22
Household Demand for Gold: Literature Review

Chapter III 76
Research Methods

Chapter IV 114
Critical Analysis of Gold Schemes in India

Chapter V 145
Household Demand for Gold: A Secondary Data Analysis using National Sample Survey (NSS) Data Series

Chapter VI 209
Determinants of Gold Demand in India: A Case Study of Kerala using Primary Data Survey

Chapter VII 269
Summary, Conclusion and Recommendations

CHAPTER I

INTRODUCTION

This study arises from a strong interest in understanding the reasons behind the significant demand for gold in India. Throughout human civilization, gold has been regarded as immensely important. It has been viewed as a treasure of kingdoms, a source of wealth for nations, and a symbol of prosperity. Additionally, gold is often associated with purity. In Plato's "Republic," philosopher kings are described as possessing the souls of ‘gold.’ Plato theorized that different metals correspond to different souls, reflecting his belief that not all citizens are born equal. A gold soul represents kings or rulers, a silver soul signifies auxiliaries, and a brass or iron soul is attributed to craftsmen (Burton, 2010). Gold embodies all the qualities of money as described by Aristotle: it is durable, does not fade or lose its shape over time, and possesses properties of portability and divisibility. Furthermore, gold has intrinsic value; its worth is independent of the value of any other object (Lee, 2009).

In addition to the state's desire to accumulate gold, households have a strong inclination to spend their income on it. Gold serves primarily as jewelry and as an investment asset for households. However, India meets its gold demand through imports from other countries, which places a burden on the balance of payments. This study analyzes the impact of gold imports on the balance of payments, the factors driving household demand for gold, the ineffectiveness of government policies in curbing this demand, and the over-utilization of gold among households.

I.1 Background

As far back as ancient times, esteemed thinkers and rulers recognized gold as possessing immense value, granting ultimate purchasing power to those who possess it. Gold has held monetary value since its early discovery and

continues to be regarded as one of the most influential metals in terms of worth. Historically, a gold standard was adopted by various countries, establishing currency values in relation to gold. Although the gold standard has since been abandoned, gold remains a valuable reserve for governments, serves as an input in numerous industries, and is viewed as an investment in jewelry among households. Especially during periods of dollar depreciation, gold is considered a 'safe haven' investment for governments worldwide (EPW correspondent, 2003).

Classical economists perceived gold as a form of luxurious consumption. The accumulation of gold symbolized prosperity. This connection between gold and prosperity is rooted in mercantilist thought, which posited that maximizing net exports was crucial for national progress. According to this view, the true measure of a country's wealth is bullionism; that is, the quantity of gold a nation possesses reflects its actual wealth. Consequently, accumulating gold was deemed essential for a strong and powerful state (C.W., 2013). The gold standard[1] was prevalent during the era of classical economists, notably Adam Smith. Thus, gold functioned both as money and as a commodity, being freely exchangeable between these two roles. The amount of gold in circulation was closely linked to price levels, with prices fluctuating based on the supply of gold in the economy. Classical economists[2] associated the value of goods with a standard of value—gold—due to its universal desirability, transportability, and stable supply. They advocated for the gold standard as a means to ensure stable money, with the policy goal of maintaining the currency's value at a specified gold parity.

[1] Gold Standard is a monetary system in which the economic unit of account is based on fixed quantity of gold. The gold standard was prevalent among the world economies in the early times. The Bretton Woods system in 1944 replaced gold standard with gold exchange standard in which US dollar was made convertible into fixed rate of gold. The gold value was worth US$ 35 per ounce. Until 1971, the dollar was officially convertible into gold and it was abandoned in 1971. (For more details refer, Balachandran, 1989).

[2] Classical economists believed that central bank alone controls the price of gold. The price of gold is an informative variable to the central bank regarding the money demanded in the economy. They believed that even if countries resort to paper currency, gold as a measure of stable value of money remain intact. Price of gold = (supply of money/demand for money)/(supply of gold/demand for gold).

David Ricardo, in his book 'The Principles of Political Economy and Taxation,' stated that

> *"On these principles, it will be seen that it is not necessary that paper money should be payable in specie to secure its value; it is only necessary that its quantity should be regulated according to the value of the metal which is declared to be the standard."*

This logical assertion stems from the belief that gold serves as a measure of value for money, influencing any currency (Shipman, 2017). Classical economists unanimously supported a gold standard system. They linked the demand for gold to economic prosperity, while the Keynesian school associated it with socio-economic backwardness. Keynes opposed the gold standard and advocated for Great Britain's abandonment of it.

The inflation of paper currencies during the world wars prompted many countries to abandon the gold standard. The Bretton Woods system established in 1944 replaced it, making the US dollar convertible into gold at a fixed rate of $35 per ounce. This system was initiated under President Franklin Roosevelt and lasted until Richard Nixon ended it in 1971 (Mohamad, Sharifah; Masih, Mansur, 2013).

Additionally, numerous countries addressed balance of payments issues by submitting their gold reserves to multinational organizations or creditor nations. Gold is a tangible asset that countries utilize to meet their debt obligations. In the early 1990s, India faced an external sector crisis, with foreign exchange reserves sufficient for only two weeks of imports. This crisis resulted in a downgrade of the country's credit rating by international agencies. Exogenous factors negatively impacted export growth while simultaneously increasing interest rates (Sen, Sunanda, 1994). However, Nayar (1998) argued that the crisis stemmed from prior economic policies rather than external shocks. Current expenditures had outpaced revenues, leading to significant fiscal deficits after the 1980s. The government sold 20 tonnes of reserve gold for $200 million, alongside securing IMF loans and SDRs. Thus, gold continues to be a valuable asset for governments worldwide.

Although gold is no longer used as currency, its value as an asset remains strong. Countries worldwide still regard gold as a crucial component of their financial reserves. This principle also applies to households, particularly in developing nations like India and China.

World Gold Demand

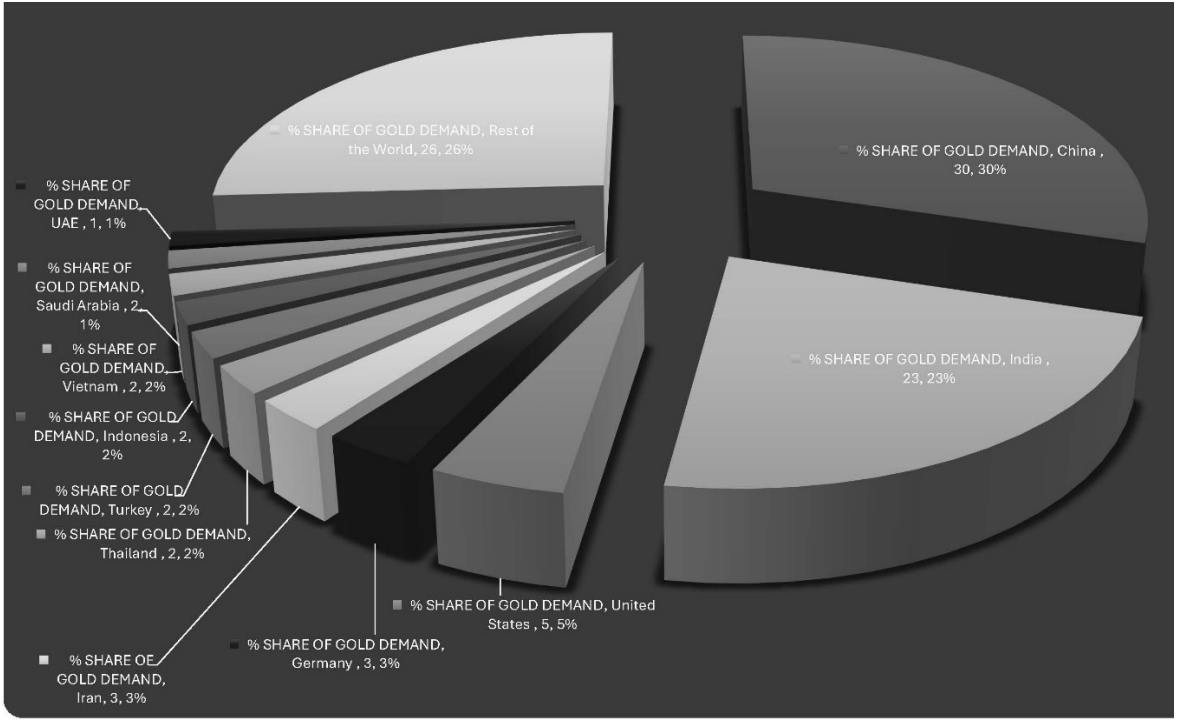
Table I.1 provides an overview of the top countries demanding gold. In 2018, the total world demand for gold was reported at 3,332 tonnes, with the eleven nations listed accounting for roughly 74% of this global demand. Among these nations, the combined demand from China and India constitutes about 53% of the total. Specifically, China demanded approximately 30% of the world's gold, amounting to 994 tonnes, while India accounted for 23%, or 760 tonnes. Other countries, such as the United

TABLE I.1: SHARE OF GOLD DEMAND AMONG COUNTRIES (2018)

	Country	Tonnes	% SHARE
1	China	994	30
2	India	760	23
3	United States	154	5
4	Germany	107	3
5	Iran	91	3
6	Thailand	81	2
7	Turkey	74	2
8	Indonesia	64	2
9	Vietnam	60	2
10	Saudi Arabia	50	2
11	UAE	42	1
	Above Total/average	2477	74
	World	3332	100

Source: World Gold Council Report, 2019.

GRAPH I.1: % SHARE OF GOLD DEMAND (2018)



Source: World Gold Council

States, Germany, and Iran, had demands of 154, 107, and 91 tonnes, respectively. Additionally, countries like Thailand, Turkey, Indonesia, Vietnam, and Saudi Arabia each demanded 2% of the total gold demand in 2018. This data clearly indicates that more than half of the total demand for gold originates from India and China, both of which are developing countries marked by low per capita income and significant income inequality.

In India, household demand is the primary driver of gold consumption. A small fraction of gold is produced domestically in the Kolar gold fields; the majority of the demand is satisfied through imports. India ranks just behind China in terms of its share of total world gold demand. The continually rising demand for gold places significant pressure on the country's current account deficit. Despite strict import restrictions, a considerable amount of gold often enters the country through illegal channels. This high demand for gold exerts substantial pressure on India's balance of trade and current account balance. Furthermore, households tend to allocate their savings toward unproductive gold consumption, which intensifies the challenges faced by an already capital-scarce economy.

A study by the Reserve Bank of India on household savings (2014) revealed that financial assets make up only one-third of household savings in India. In contrast, savings in physical assets such as gold and real estate account for two-thirds. The late 1960s saw a low ratio of financial to physical savings, attributed to a combination of interest rates and a surge in real estate and gold investments, which encouraged people to shift their savings toward physical assets[3].

The National Council for Applied Economic Research (NCAER) study (2016) examined the savings patterns of Indian households using data from the All India Debt and Investment Survey (AIDIS) 2012. It provided evidence on how fluctuations in macroeconomic variables affect household wealth allocation, particularly regarding gold holdings. In 2011-12,

[3] Financial savings decreased from 46 percent in the financial year 2001 to 32 percent in the financial year 2013. During the same period, physical savings rose from 5 percent to 68 percent. (RBI Report of the Working Group on Savings During the Twelfth Five-Year Plan, 2012)

approximately 70 percent of aggregate annual household savings were directed toward physical assets. The study reached several key conclusions: Inflationary hedging motives significantly influence households' precautionary savings. Experiences with inflation have a stronger explanatory power for gold allocation. Additionally, education has a marked effect on the proportion of household savings allocated to financial investments, with findings indicating that the non-financial ratio decreases as education levels rise.

TABLE I.2: HOUSEHOLD SECTOR SAVINGS RATES (AS PERCENTAGE OF GDP AT CURRENT MARKET PRICE)

Sl. No.		1950	1960	1970	1980	1990	2000	2004	2016
1.	Household sector	7	8	12	15	19	21	22	25
2.	Financial Savings	2	3	5	7	10	10	10.3	12
3.	Physical assets	5	6	8	8	9	11	12	13
Source: Planning Commission, RBI									

Current Account and Gold Demand

Gold imports adversely affect current account deficits. Furthermore, the substantial demand for gold diverts household savings that could otherwise be invested in productive assets, which would support economic growth. Thus, high demand for gold not only impacts the country's balance of payments but also diverts investments away from productive sectors, ultimately hindering economic development.

In 1994, India's total gold stock was estimated at 9,016 tonnes, accounting for about 7 percent of the world's total gold reserves. The annual gold demand in India was approximately 16.4 percent of the global total. However, India produced only 0.09 percent of the world's gold demand, amounting to just 2 tonnes compared to the 2,272 tonnes supplied globally. As a result, the majority of India's gold demand was satisfied through imports. The price differential between Indian and international markets

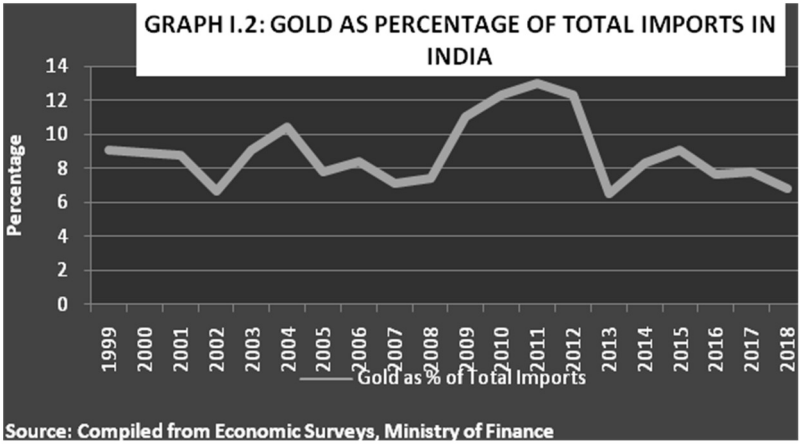
was higher prior to liberalization and decreased during the post-liberalization period due to changes in the exchange rate regime and relaxed import restrictions. In the absence of open imports, domestic gold prices relative to international prices were influenced by two main factors: "(i) the spread between the official and market exchange rate of the rupee, and (ii) customs duty, transportation costs, storage costs, risk premiums, etc." (Reddy Y.V., 1996).

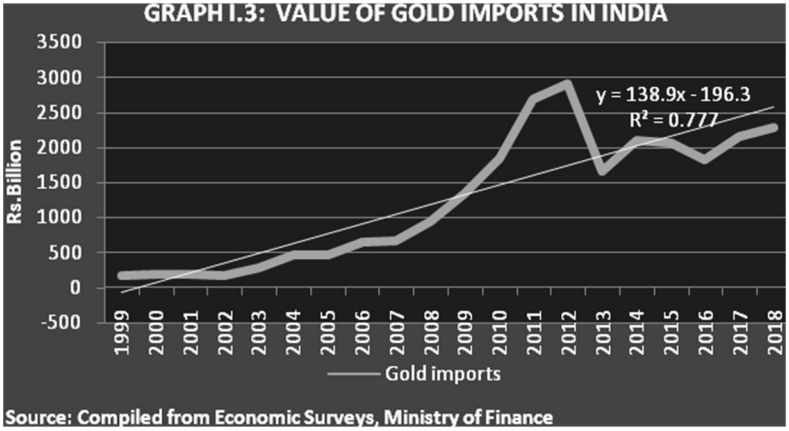
India has a long history of gold imports. A. Vaidyanathan (1998) noted that gold imports have not increased in a linear fashion. There was a significant influx during the Great Depression of the 1930s. Average annual demand was comparatively lower during the periods of 1941-50, 1958-63, and 1974-80. Even after a ban was imposed in 1947, gold imports rose to 80–90 tons per year. Following the ban's removal in 1992, annual imports surged to 399 tonnes. A Gold Council study (2004) indicated a substantial increase in gold consumption in India post-liberalization, rising from 200 tonnes to between 500 and 600 tonnes annually after official deregulation began in 1990.

Dhar and Rao (2014) indicated that India's trade deficit widened after 2000, primarily due to broad tariff reductions resulting from comprehensive economic partnership agreements (CEPA) and an increase in imports driven by gold and crude petroleum products. As gold imports reached high levels, customs duty was raised to 4% in the 2012 budget. Although restrictions and the anticipation of further restrictions led to a decline in official gold imports in 2013, the growing demand was fulfilled through unofficially smuggled gold. In the period from October to December 2012, excluding the influence of gold from total imports, the import ratio decreased by 3.6 points to 23.4 percent. Consequently, the trade deficit fell from 12.3% to 8.6%, and the current account deficit decreased from 6.7% to 3% of GDP (Krishnaswamy & Kanagasabhapathy, 2013).

The EPW Research Foundation (2005) also estimated that over 1.5 percent of GDP was being diverted into unproductive asset holdings, at a time when the economy's domestic saving and investment rates had remained effectively stagnant at around 23 to 34 percent of GDP.

Graph I.2 illustrates the share of gold in total imports in India from 1999 to 2018. Notably, during the 2009–2012 period, there was a significant increase in the share of gold in the country's total import bill, rising to 11 percent in 2009 and peaking at 13 percent in 2011. By 2018, gold imports accounted for approximately 7 percent of the total import bill.





Graph I.3 illustrates the value of gold imports in India for the period from 1999 to 2018. Notably, the curve consistently rose, reaching a peak value of Rs. 2922 billion in 2013. Following this peak, the value decreased to Rs.

1662 billion in 2014 but displayed an upward trend thereafter. In 2018, the value of gold imports was Rs. 2295 billion. The trend line indicates that, on average, the value of gold imports increases by Rs. 138 billion each year.

Gold Deposit Schemes

Excessive demand for gold indicates that a portion of black money is stored in bullion or jewelry (EPW, 1997). Smuggled gold accounts for approximately 70 to 80 percent of India's total gold demand. To address this issue, the government has introduced gold deposit schemes at various times, aiming to utilize the gold held by households and reduce the import burden. The value of private gold holdings in the country is more than four times that of foreign exchange reserves (EPW correspondent, 1999). However, these gold deposit schemes have only managed to capture a small share of the overall gold demand.

The government's policy allowing the legal import of gold seeks to minimize illegal foreign exchange transactions, combat the 'hawala' market, and generate customs revenue. This policy has stimulated gold consumption. Furthermore, domestic savings financed the majority of gold imports—around 300 tonnes annually, valued at approximately Rs. 14,000 crores in 1995 (EPW Correspondent, 1995).

I.G. Patel expressed skepticism about the effectiveness of gold bonds, suggesting they might become a tool for tax evasion. He believed the solution lies in "a mixture of sustained propaganda, compulsion, and incentives affecting people's expectations about the value of gold in the future" (Chandavarkar, 2006). Patel estimated the price elasticity of gold to be 1.6 relative to the consumer index during 1952–1959. Madan posited a high income elasticity of demand for gold, noting that demand typically rises in times of agricultural prosperity.

The gold control policy established since independence has concentrated on five primary objectives: (a) to divert people away from gold, (b) to regulate the supply of gold, (c) to prevent smuggling, (d) to decrease demand for gold, and (e) to lower domestic gold prices. According to Reddy (1996), gold prices do not significantly influence demand for most people, as gold

is regarded as a safe haven for investing black money.

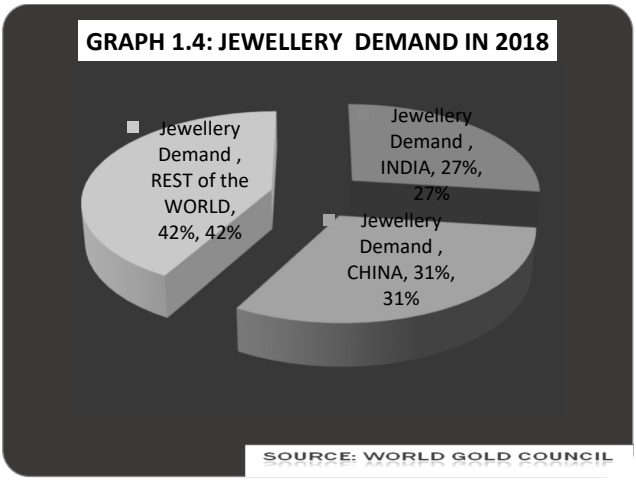
Household Demand

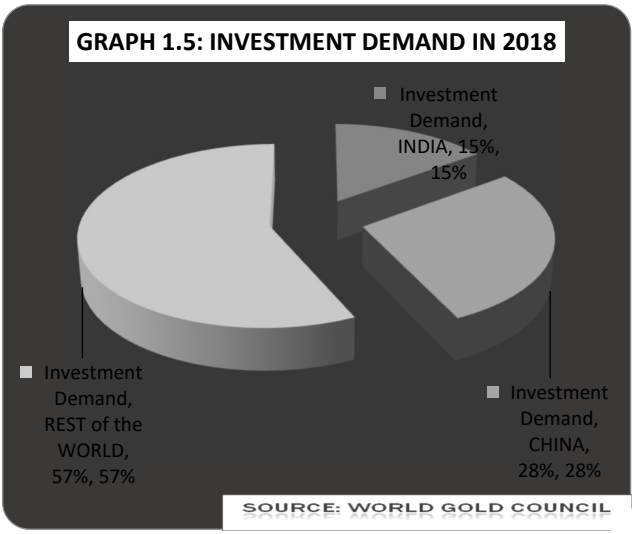
In India, most gold demand stems from households, with approximately 80 percent of the demand originating from Indian households themselves (see Table I.3). In 2018, the global demand for gold in the form of jewelry accounted for 67 percent. Of this, Indian households contributed about 27 percent to the total world demand for jewelry. Together, India and China accounted for 58 percent of the overall jewelry demand for gold globally. In terms of investment demand for gold, which includes gold bars and coins, India represented about 15 percent, while China accounted for approximately 28 percent in 2018.

TABLE I.3: GOLD DEMAND IN 2018

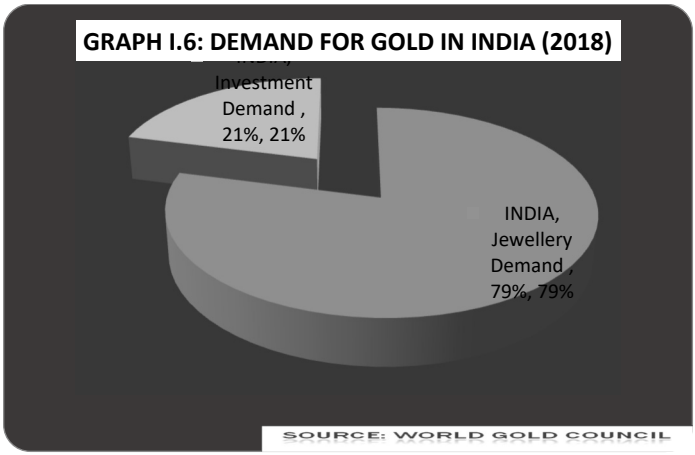
		WORLD		INDIA		CHINA	
Sl. No.		**Tonnes**	**% share of total demand**	**tonnes**	**% share of total demand**	**tonnes**	**% share of total demand**
1	**Jewellery**	**2241**	**67%**	**598**	**79%**	**686**	**69%**
2	**Investment Demand (Bar & coin)**	**1091**	**33%**	**162**	**21%**	**308**	**31%**
3.	**Total Consumer Demand**	**3332**	**100%**	**760**	**100%**	**994**	**100%**

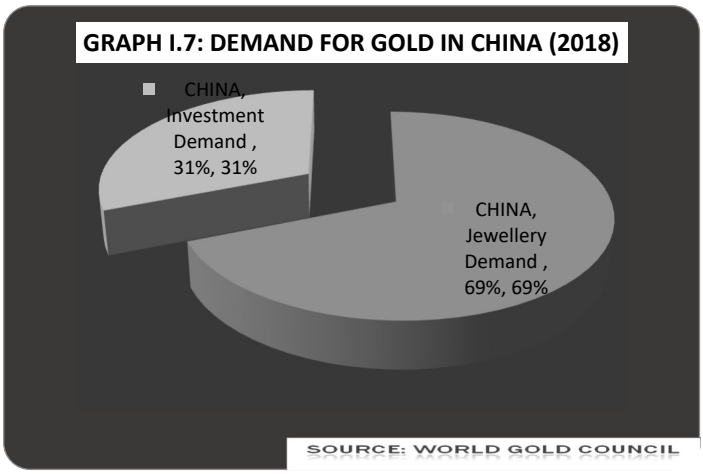
Source: Gold Demand Trends 2019, World Gold Council.





Graphs 1.6 and 1.7 illustrate the demand for gold in India and China during the year 2018. In India, the demand for gold jewelry was the highest globally, accounting for approximately 79 percent of the total demand. In contrast, the investment demand for gold in China, which includes gold bars and coins, was nearly equal to the world average. However, India's investment demand for gold was only 21 percent, while the world average stood at 33 percent in 2018.





The share of gold ornaments in household durable expenditure was approximately 24 percent in rural India and 20 percent in urban India (NSSO, 2014). The primary drivers of household demand for gold stem from its ever-increasing value, serving as a hedge against inflation, as well as various socio-economic and cultural factors.

Vaidyanathan (1999) dismissed any motivation for holding gold beyond financial hedging and speculation. He analyzed gold demand using the ratio of gold prices to the GDP deflator, the price of ordinary shares, the foreign

price of gold, real GDP, and the household financial savings rate. He concluded that the price of gold relative to share prices and international gold prices significantly influences gold imports. He argued that as long as the exchange rate and gold imports are determined by market forces, share prices will likely become the primary determinant of gold imports. His analysis primarily focused on the investment-side demand for gold, noting that the number of Indian households participating in the stock market is minimal. Omkarnath (1999) highlighted the roles of speculators, money launderers, and merchants in driving increased demand for gold.

N. Madhavankutty (2013) explored how the timing of gold demand accumulation in households is affected by the institution of dowry. He found that demand for gold tends to be lower in regions with lower dowry practices, contrasting examples from low-dowry and high-dowry states in India.

Classical economists viewed gold consumption as a marker of prosperity, attributing it to rising real incomes. In contrast, Keynesian economists interpreted it as an indicator of socio-economic backwardness. Empirical studies have shown relevance to the 'Veblen effect' in the context of gold, indicating a negative price elasticity for gold demand. Expectations of rising prices have had a significantly positive impact on gold demand (Mani and Vuyyuri, 2003). Gold is commonly regarded as a hedge against inflation (Capie et al., 2004). People use gold as a tool for saving and as an alternative to risk-free bank deposits and government bonds. Dalglish (1993) suggests that higher opportunity costs make individuals less inclined to save in gold.

India's gold demand function has been estimated concerning both aggregate gold demand and the demand for gold fabrication and jewelry. This demand function is influenced by several factors, including real income, relative gold prices, interest rates, equity prices, exchange rates, personal income tax, and government spending. The results indicate that gold demand is sensitive to price changes and is also affected by macroeconomic and financial variables. Dhal and Kannan (2008) argued that examining the productive asset utilization of gold has substantial implications for policy research.

The household demand for physical assets rose from 11.4 percent of GDP in 2005–07 to 13 percent by 2008–10. Simultaneously, net financial assets decreased from 11.6 percent to 11 percent during the same period. This trend illustrates a clear shift among households from financial savings to physical assets, largely driven by low real interest rates on deposits, which have resulted from high inflation and stock market disruptions (RBI, 2012). Srivatsava (2013) highlighted that Indian households primarily favor gold due to its dual role as a medium of exchange and a store of value. Gold generates interest when lent and has outperformed inflation by a margin of 400 basis points over a 40-year period from 1970 to 2010.

Dhar and Rao (2014) noted that uncertainty in real estate and equity markets has made gold an appealing investment, serving as an effective hedge against inflation. Consequently, efforts to reduce gold demand should focus on creating new financial instruments that can deliver real returns. The World Gold Council's suggestion to monetize gold as a financial asset is relevant in this context. Chandavarkar (2006) applied IG Patil's analysis of price elasticity to the current situation, concluding that a 20 percent increase in gold prices would turn India into a gold-exporting country. He explained the reasons behind the stable price of gold in India, noting that a significant portion of the gold supply is smuggled. Changes in supply prices primarily affect the profits of smugglers without impacting the actual market price. The rupee price of gold remains stable regardless of the demand curve's nature. The EPW Research Foundation (2005) highlighted that a substantial increase in import duties and the implementation of wealth taxes are likely reasons for shifting public preference from gold to financial assets.

I.2 Statement of the Problem

There is no doubt that gold imports contribute to an increase in the current account deficit (CAD) of the country. The existing literature and data indicate the influence of gold on current account deficits; however, there is a lack of detailed analysis regarding the role of gold in these deficits.

Over time, governments have attempted to reduce gold demand in India by introducing various policy measures and financial instruments. However, these initiatives have generally failed to gain traction in the market,

including recent programs like the Gold Monetization Scheme introduced in 2015. There is a lack of comprehensive studies examining the reasons behind the failure of government schemes aimed at curbing gold demand in India, as existing research primarily focuses on outlining these schemes.

The National Sample Survey (NSS) offers detailed data on durable asset consumption in households, including annual data and monthly per capita consumption expenditure. Gold ornaments are categorized as durable assets. Nonetheless, there are no studies that adequately analyze the reliability of these secondary databases concerning gold demand and durable asset consumption in India. Additionally, there is a notable research gap in the literature concerning the identification and prioritization of the factors driving household demand for gold in India. This study aims to address the aforementioned gap in existing literature.

I.3 Research Problem/Question and Hypothesis

A wide range of research question arises about the ever-increasing consumption of gold in India.

i) A wide range of gold control policies had been experimented with by the government. What is the reason behind the non-functioning/bad performance of such control policies?

Null Hypothesis: Gold control policies by the government failed to curtail the demand side of gold, and so it led to the disastrous performance of such policies.

(ii) What factors determine the demand for gold in India? Is it more influenced by socio-cultural aspects rather than socio-economic ones? or socio-culturally oriented rather than socio-economically?

Null Hypothesis: Socio-cultural reasons are more determining in the demand for gold than the socio-economic factors.

(iii) Gold accumulation by households is always considered as an investment by them for unproductive purposes. Do they never utilize gold for productive purposes?

Null Hypothesis: Gold is just hoarded with the households as a physical asset, and there exists no utilization of gold for productive purposes.

I.4 Objectives

It is a well-established fact that Indian households have increased their demand for gold in recent years compared to earlier periods (NSSO, 2014). The demand boost may be driven by the characteristics of gold as a store of value as well as powered by many other factors, including socio-cultural factors. Since gold is majorly used as an ornament, a case of the Duesenberry effect also cannot be nullified. Whatever the determinants of demand for gold, its impact on the country's balance of payment as well as erosion of savings cannot be undermined. In this context that the objective of the present study is to:

- to critically evaluate the effectiveness of gold policies on the demand for gold in India;
- to analyze the state-wise gold consumption expenditure over the period of time;
- to analyze the determinants of gold in India based on secondary data sources; and
- to analyze the determinants of gold based on the primary data survey in Kerala, where gold is largely demanded in India.

I.5 Definition, Rationale and Scope of the Study

Gold consists of all forms of pure gold bars, gold coins, gold jewellery, raw gold, etc. So, total demand for gold is the sum total of all forms of gold demanded by government, industries, and households in the country.

Productive and unproductive assets: A productive asset is something that contributes to the production process in the economy. When we say that gold is an unproductive asset, it means that it is basically hoarded among the households. So it cannot participate in the production process.

The present study is expected to throw light on the existing knowledge on the determinants of gold demand in the country. It will also address the

present gap in the literature over the utilization of gold among households.

The scope of the study is not only limited to the economic aspect of gold demand but also stresses the non-economic factors and anti-social activities, such as the role of the dowry system in constituting gold demand.

I.6 Research methods

Research methods likely to be chosen were mostly quantitative in nature. The data set consists of both secondary data and a primary survey. Secondary sources of data sets consist of the National Sample Survey (NSSO), RBI, etc.

NSSO surveys explain the details of household consumption expenditure on durable goods. Gold accounts for 24 percent of total expenditure on durable goods in rural India; in money terms, it is valued at Rs.25,081 per year. A boost in gold expenditure was noticed in the 2011-12 period, i.e., from 14 percent to 24 percent in rural India. A state-level analysis based on NSSO data sets to reveal the reasons for increased demand for gold will be one of the prime objectives of this study.

Selection of sample population: The sample population for the primary survey shall be selected based on the largest gold-demanding state in the country. Currently it is Kerala. Kottayam district is selected as the sample collection area; the choice is based on its characteristic as one of the most gold-consuming districts in Kerala. The following table provides the population profile of Kottayam district. Kottayam accommodates 6 percent of the total population in Kerala. The characteristics of Kottayam District differ widely as compared to the whole of Kerala, i.e., in the case of religious groups and rural/urban characteristics. But the sample from the district will be selected based on the proportionate share of these characteristics in Kerala, i.e., the sample should consist of 52% of the rural population and 56% of Hindus, followed by 25% of Muslims and 19% of Christians, irrespective of the population profile of Kottayam district.

Sample size: Currently, the chosen sample size is 300 households based on the feasibility and affordability of cost and time characteristics.

The cluster sampling method will be utilized, incorporating a mix of below-poverty-level and above-poverty-level households, as well as a religious composition that includes Hindus, Christians, and Muslims. Additionally, households will be categorized into General, Scheduled Castes (SC), and Scheduled Tribes (ST).

Selection of Sample Households: In the Kottayam district, which encompasses both urban and rural areas, there are 73 villages governed by 11 panchayat blocks representing the rural regions, alongside 4 municipalities representing the urban portion. A detailed list of block panchayats and municipalities can be found in Annexure II. Among the 300 households selected, the ratio of rural to urban households is 13:12, meaning that for every 13 households chosen in rural areas, 12 households will be selected in urban areas.

Samples will be selected using scientific sampling methods. The primary survey will be conducted using questionnaires through face-to-face interviews. The results will be analyzed statistically using techniques such as percentages, correlations, and regression analysis.

TABLE I.4: ALL INDIA YEARLY CONSUMPTION OF GOLD ORNAMENTS

Sl. No.		Rural	Urban
1.	2004-05	13.8	11.5
2.	2009-10	14.2	14.3
3.	2011-12	23.6	19.9
Expenditure in last 365 days (Rs.) in 2011-12		25081	27855

Source: Household consumption of Various Goods and Services in India: 2011-12, NSSO, Ministry of statistics and Programme Implementation. Govt. of India.

TABLE I.5: PROFILE CHARACTERISTICS		
	Kerala	Kottayam
Rural:Urban	1:1	3:1
SC/ST:Gen	1:9	1:10
Hindu:Muslim:Christian	3:1:1 (approx)	8:1:8 (approx)
BPL:APL	1:4	1:4
Source: Census 2011, Office of the Registrar General & Census Commissioner, Govt. of India		

TABLE I.6: POPULATION PROFILE					
		Kerala		Kottayam	
Sl. No			% share		% share
1.	No. of households	7703616		487296	6%
2.	Total Population	33387677		1974551	6%
3.	Rural	17455506	52%	1409158	71%
4.	Urban	15932171	48%	565393	29%
5.	SC	3039573	9%	153909	8%
6.	ST	484839	1%	21972	1%
Religious Compositions*					
7.	Hindu	17883449	56%	963497	49%
8.	Muslim	7863842	25%	116686	6%
9.	Christian	6057427	19%	871371	45%

Income Compositions					
10.	Antyodaya Anna Yojana (AAY)	576056	7%	33945	7%
11.	Below Poverty Level (BPL) Households	1476841	19%	95250	20%
12.	Above Proverty Level (APL) Households	6207717	81%	371739	76%
Source: Census *2001 & 2011, Office of the Registrar General & Census Commissioner, Govt. of India					

CHAPTER II

HOUSEHOLD DEMAND FOR GOLD: LITERATURE REVIEW

Classical economists believed that demand for investment is a derived demand and any factor of production is demanded for its 'productivity only. Demand for savings arises from those who want to invest in productive activities. The demand for capital is up to a point where its marginal productivity is equal to the interest paid for it. There exists an inverse relationship between rate of interest and investment. Savings is the main source of capital. Savings depends on capacity to save and willingness to save. The willingness to save further depends on the rate of interest. The higher the rate of interest, the more people will save. So, there is a positive relationship between savings and rate of interest.

According to Keynes (Keynes, 1936), there exist eight motives to save, which include uncertainty or precautionary motive, foreseen changes in income in relation to anticipated needs (i.e., life cycle), time preference (i.e., inter-temporal substitution), to enjoy gradually increasing expenditure, to enjoy a sense of independence, to carry out speculative business, to provide a large inheritance, and people may also save out of avarice. Keynesian theory is a below-full-employment model. When savings is greater than investment, the level of income in the economy decreases and causes savings to decline. This causes savings equal to investment at below full employment. Keynes's absolute income hypothesis (Alimi, 2013) states that when income increases, consumption also increases but not as much as the increase in income[4].

[4] Keynesian Consumption Function = C = a + bY, where 'a' is autonomous consumption, which is independent of the level of income. According to Keynes, the average propensity to consume (APC) is lower than the marginal propensity to consume (MPC). The MPC is constant, and the APC declines when income increases.

For a theoretical understanding of the huge demand for gold in India, one should start with the savings and wealth allocation pattern in the country. The household income is supposed to be either consumed or saved. Savings is considered the postponement of current consumption. It is the excess of income over expenditure on consumption. The saving of the household income may be in cash itself or in the form of a financial asset or as a physical asset such as gold, land, etc. Here, the primary motive of the study is to analyze the savings pattern of households in physical asset format, especially gold. Savings-income identity can be written as:

Y = C + S, where Y is the household income, C is the consumption expenditure of households, and S is the savings of the household.

S = Y-C; the remainder of income that is not used for the household consumption is the savings of the households.

Savings by household sector is defined as "that payment of current income after payment of taxes, which is not consumed or transferred as part of household current consumption." Savings is divided into contractual and discretionary savings. The former is individual commitments to a series of payments, such as insurance policies, and the latter is the type of savings in which households are not bound by any fixed commitments (Prinsloo, 2000). Farrell (1959) tried to distinguish the theories of consumption put forward by Friedman, Modigliani, and Brumberg. Current income is the total of the individual's receipts during the year, including earnings and interest yield on assets. Savings are the accounting difference between current income and consumption. The purchase of consumer durables is considered a capital expenditure, whereas consumption of durables is the current cost, i.e., depreciation plus interest costs. **The normal income hypothesis states that an individual' current income y affects his consumption c only through its 'effect on normal income ϒ. So c = β (ϒ),** where β is independent of current income and assets. For people with variable incomes, the normal income hypothesis is equivalent to postulating a rational behavior, but people with stable incomes may follow 'save 1/nth of income.

According to the proportionality hypothesis, the relationship between consumption and normal income is proportional. Under this hypothesis, consumption includes durable purchases, too. **The proportionality hypothesis states that each consumer's consumption varies proportionately with his income.** The rate of growth hypothesis states that in the long run, the fraction of aggregate income saved is proportional to the rate of growth of aggregate real income. The correlation of normal income with age, magnitude, and temporary fluctuations is positively correlated with current income. Friedman, in his occupational survey, found that in higher current income groups, normal income increases less than proportionately with current income, and thus the elasticity of normal income with respect to current income (F) is less than one. This is called the Friedman effect (F<1), and this is applicable to some social groups.

Rutherford (2000), in his book 'The poor and their money,' ascertains that poor people lack savings accounts, and like anyone, they are also well inclined to save their little wealth from inflation. The poor are very intrigued by forming self-help groups. But a survey by Banerjee and Duflo (2006) found that only less than 10 percent of the poor in Udaipur and Hyderabad were found to have any savings account with self-help groups.

Savings depend upon the ratio of income and wealth. **Crammer (1962) stated that income and wealth are the important determinants of ownership of durable goods.** His analysis in 1953, based on data collected from the Oxford savings survey, referred to the ownership of four major domestic durable goods, such as motor cars, refrigerators, washing machines, and television sets. A bivariate distribution function was fitted over the distribution of income and net worth. But Crammer's work was not fulfilled in the sense that the variables of income and net wealth cannot be claimed as more important determinants of ownership of durables. Crammers work ignored the problems of choice faced by the household in accumulating durable goods. **Pyatt (1964), in his work on demand for consumer durables, stated that stockholdings rather than consumption are the motive for demand for durable goods.**