

# Central Bank Digital Currency (CBDC) and Gold Trade in India

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(The view shared here are Author's own)

In a country where cash still dominates the gold and jewellery trade, it is natural to have some apprehensions about how the CBDC will impact the gold and jewellery trade. A lot depends on the design choice and the degree of anonymity on the rollout of CBDC.

clearly spelled out, the Indian digital currency (e₹) will complement the currently available forms of money, implying that the e₹ is in no way, at least at this time, intended to replace the existing forms of currency and is positioned as a convenient alternative to the physical notes.

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## Background

Public interest and safeguarding public trust in money remain the topmost priority of all the Central Banks while rolling out CBDC projects. Being able to maintain trust in the financial system requires that the Central bank have the right degree of influence and direction, creating powers on the currency and the monetary system. In recent times, perhaps, no other item has shown the possibility of not only enhancing the influence, directionality, and visibility but also increasing the efficiency of the use of money as crypto – or, more specifically, a form of it now known as Central Bank Digital currency (CBDC) – a form of digital money issued by a Central Bank.

Technology innovations in payment solutions have always been one of the thrust areas of Central Banks around the globe. RTGS, NEFT, or instant payment solutions like IMPS

and UPI have been game changers in many ways. The changing pattern of spending and, to some extent, the growing attention towards private decentralized cryptocurrencies and their likely impact on a country's monetary policies and financial stability has motivated many Central Banks across the globe to start exploring the issuance of CBDCs. While the deliberations around CBDCs were started way back in 2014, it has gained momentum in the last couple of years. The purpose of introducing CBDC includes improving efficiency in the financial system, not falling behind leading economies when the Indian fintech stack is already world-leading, and continuing, while keeping these goals in mind, to retain the trust of financial markets and the public in money and the monetary system.

The Reserve Bank of India released its concept note in October 2022. As

RBI envisaged a phased implementation of e₹ starting with the pilot runs of wholesale e₹, followed by the pilot run of retail e₹ before the final launch. In a country that has seen demonetisation of currency notes not so long ago, any such initiatives by the regulatory authorities to make money that can be configured can be seen with some skepticism or trepidation. Through the concept paper, RBI has ensured that the rollout of e₹ will not disrupt the existing payment system. RBI has also clarified that the sovereignty of the currency will not be impacted in any manner while changing the currency shape from physical to digital. An offline feature is proposed that will help smooth and uninterrupted operations even in the remotest locations.

## Objectives

In line with the guiding principles laid down by the International Monetary Fund (IMF) and Bank of International Settlement (BIS), RBI's CBDC is aimed to achieve the following broad objectives:

- Reduction in operational costs

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CBDC is aimed to complement, rather than replace, current forms of money and is envisaged to provide an additional payment avenue to users, not to replace the existing payment systems.<sup>1</sup>

of issuance and management of currency

- Nurturing financial inclusion
- Bringing efficiencies in the payment and settlement system
- Facilitating cross-border trade
- Efficiency in cross-border transactions/ settlement
- Providing all the possible benefits of physical notes without the associated risks relating to their possession
- Ease of operations and user experience at par with private cryptocurrencies, with the sovereign guarantee and eliminating the risks to the stability of the country's financial structure.

#### Key design choices

- Wholesale CBDC is meant for banks and Financial Institutions to settle interbank transfers and related wholesale transactions. Retail CBDC is targeted at non-financial consumers & businesses and can be categorized as the electronic version of cash. When should which one be introduced at scale? What should be the decision criteria?
- The CGDC can be directly managed where RBI manages its issuance, account keeping, and transaction verification. Alternatively, it can be an indirect management system at par with the present system of banknotes management, where banks manage the distribution, KYC/ AML/ CFT, account management, and transaction monitoring.
- Another design choice is between a token-based or an

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account-based system. Under a token-based system, the CBDC is a digital token and bearer instrument. The holder of the token is the owner, just like banknotes. The account-based system is an online system managed by an intermediary and is more suitable for wholesale CBDC, whereas the former is for retail. Token-based systems would have greater anonymity and, from a behavioral standpoint, greater acceptance among individuals.

- Instrument design can be remunerated where the holder earns interest like a bank deposit. A non-remunerated design replicates the present cash system where the holder gets the interest only when he issues instructions to deposit

his holding in a bank to earn interest.

- The key design feature, the most significant trade-off for the authorities to design, is the degree of anonymity and ownership. The physical banknotes today ensure absolute anonymity, which is impossible to achieve in any form of CBDCs as the digital transaction will always leave a trail. It depends on how much the authorities want to control and the objective for the same. It is also possible to stipulate that if the money is not spent by a specific time, it will become worthless – decreasing the level of ownership by the person holding the CBDC; this could be problematic.

<sup>1</sup>RBI CBDC: Digital Rupee pilot starts from November 1; SBI, HDFC, 7 ....  
<https://economictimes.indiatimes.com/wealth/save/rbi-cbdc-digital-rupee-pilot-to-start-from-november-1-sbi-hdfc-7-other-banks-to-participate/articleshow/95205659.cms>

## CBDC and gold and jewellery trade in India

In a country where cash still dominates the gold and jewellery trade, it is natural to have some apprehensions about how the CBDC will impact the gold and jewellery trade. A lot depends on the design choice and the degree of anonymity on the rollout of CBDC. The following points, however, merit consideration:

1. Currently, there are reporting requirements for high-value transactions under the Income Tax Act and PMLA under FATF guidance. Gold transactions over Rupees two lacs require furnishing the buyer's PAN card under rule 114B of the Income Tax Act. If the threshold limit for transaction disclosure remains the same, nothing changes for gold and jewellery trading transactions within this limit.
2. The size of the organised jewellery trade has been on the rise consistently over the years. The WGC report suggested that the share of chain stores in the jewellery trade rose to around 35% in 2021. It is pertinent to note that many buyers opting to purchase from stand-alone stores are not transacting due

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***Over the last decade, the retail jewellery market has undergone a notable shift, driven by changes in consumer behaviour and government regulations designed to encourage the industry to become more organized<sup>2</sup>.***

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to anonymity but because they keep the family tradition of buying from their trusted family jeweller.

3. Cash is still the king when it comes to buying gold & jewellery at the retail level. As per WGC estimates, cash accounted for about 67% of gold purchases in 2018 and 2019. However, it will not be fair to assume that majority of the cash transactions in gold and jewellery happen due to anonymity. A large percentage of these transactions are not reflective of unaccounted transactions. A GST-paid invoice backs a bulk of cash purchases happening at large retail stores. The cash purchases in the rural markets are on account of their cash earnings from agriculture, which is tax-exempt in any case.
4. As things stand now, the Central Banks across the globe, including RBI, seem to be in sync with the idea of implementing a CBDC, which is not intended to eliminate physical cash altogether. Unless there is an extreme change in the thinking process backed by a solid reason to choose the extreme design form, there is not likely to be any negative impact on the gold market.
5. There is also the potential impact of the CBDC on the cash flow cycle of the jewellers. The current gold movement mechanism between the foreign exporter, nominated agency, and the jeweller is based on a credit system that could become wholly non-required?

## Conclusion

The Bahamas, the first to roll out the CBDC, has adopted a three-tiered anonymity approach. The first-tier transactions of a small amount (\$500 with an overall \$1,500 a month) held in the wallets are not under any kind of regulatory scrutiny. The next tier, up to \$10,000 monthly, requires an official ID. Transactions above that threshold require the highest degree of disclosure. China has also adopted a similar approach of 'controllable anonymity'.

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***"ANONYMITY FOR SMALL VALUE AND TRACEABLE FOR HIGH VALUE,"***

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One key challenge for all Central Banks in implementing CBDC is due to no precedence and the requirement of extensive stakeholder consultation and managing expectations. A larger challenge will be on the retail side, where behavioral changes are required from individual holders of the CBDC. Like other failed schemes like the Gold Monetization Scheme, retail CBDC will fail unless the behavioral change requirements are addressed and managed through appropriate interventions. Without these interventions, adoption will not happen or will happen in a timeframe that makes the rollout ineffective at best and a complete failure at worst. Regarding India's gold trade, some degree of short-term impact on gold and jewelry trading cannot be ruled out based on the design and the extent of the transactions covered under CBDC. However, any kind of transparency in the trade has long-term benefits for the overall development of the trade. It will facilitate achieving the objectives of gold's financialization. ■■■

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<sup>2</sup><https://www.gold.org/goldhub/research/jewellery-market-structure-india-gold-market-series>

<sup>3</sup>Reserve Bank of India - Reports. <https://rbi.org.in/scripts/PublicationReportDetails.aspx?ID=1218>