Investment Instruments of Capital Market & Money Market

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INTRODUCTION

Investment is the employment of funds on assets with the aim of earning income or capital appreciation Investment has two attributes namely time and risk. Present consumption is sacrificed to get a return in the future. The sacrifice that has to be borne is certain but the return in the future may be uncertain. This attribute of investment indicates the risk factor. The risk is undertaken with a view to reap some return from the investment. For a layman, investment means some monetary commitment. A person's commitment to buy a flat or a house for his personal use may be an investment from his point of view. This cannot be considered as an actual investment as it involves sacrifice but does not yield any financial return.

To the economist, investment is the net addition made to the nation's capital stock that consists of goods and services that are used in the production process. A net addition to the capital stock means an increase in the buildings, equipments or inventories. These capital stocks are used to produce other goods and services.

Financial investment is the allocation of money of assets that are expected to yield some gain over a period of time. It is an exchange of financial claims such as stocks and bonds for money. They are expected to yield returns and experience capital growth over the years.

The financial and economic meanings are related to each other because the savings of the individual flow into the capital market as financial investments, to be used in economic investment. Even though they are related to each other, we are concerned only about the financial investment made on securities.

Thus, investment may be defined as "a commitment of funds made in the expectation of some positive rate of return". Expectation of return is an essential element of investment.

Since the return is expected to be realized in future, there is a possibility that the return actually realized is lower than the return expected to be realized. This possibility of variation in the actual return is known as investment risk. Thus, every investment involves return and risk.

Investment is a widespread practice and many have made their fortunes the process. The starting point in this process is to determine the characteristics of the various investment and then matching them with the individuals need and preferences. All personal investing is designed in order to achieve certainobjectives. These objectives may be tangible such as buying a car, house, etc., and intangible objectivessuch as social status, security, etc. Similarly, these objectives may be classified as financial or personal objectives. Financial objectives are safety, profitability and liquidity. Personal or individual objectivesmay be related to personal characteristics of individual such as family commitments, status, etc.

Characteristics of Investments

It is worthwhile considering the characteristics of some forms of investment popular amongst individuals. The most popular is probably the bank or building society deposit. On the upside these arefree of capital risk, offer an income yield, and are usually liquid. On the downside they lack substantialgrowth potential, are subject to a high level of income risk and have inflation risk.

Rental, or buy-to-let, property has become popular in recent years. Such investment has growth potential and provides an income yield. On the downside it is illiquid and subject to both income and capital risk. The income risk relates to the possibility that rents fall, or that a property fails to attract tenants and remains unoccupied for long periods. The capital risk exists because property prices can fall.

All investments are characterized by certain features. Let us analyse these characteristic features of investment.

Return

All investments are characterized by the expectation of a return. In fact, investments are made with the primary objective of deriving a return. The return may be received in the form of yield plus capital appreciation.

The difference between the sale price and the purchase price is capital appreciation. The dividend or interest received from the investment is the yield. Different types of investments promise different rates of return. The return from an investment depends upon the nature of the investment, the maturity period and a host of other factors.

Risk

Risk is inherent in any investment. This risk may relate to loss of capital, delay in repayment of capital, non-payment of interest, or variability of returns. While some investments like government securities and bank deposits are almost riskless, others are more risky.

The risk of an investment depends on the following factors.

1. The longer the maturity period, the larger is the risk.
2. The lower the credit worthiness of the borrower, the higher is the risk.
3. The risk varies with the nature of investment. Investments in ownership securities like equity shares carry higher risk compared to investments in debt instruments like debentures and bonds.

Risk and return of an investment are related. Normally, the higher the risk, the higher is the return.

Safety

The safety of on investment implies the certainty of return of capital without loss of money or time. Safety is another feature which an investor desires for his investments. Every investor expects to get back his capital on maturity without loss and without delay.

Liquidity

An investment which is easily saleable or marketable without loss of money and without loss of time is said to possess liquidity. Some investments like company deposits, bank deposits, P.O. Deposits, NSC, NSS, etc. are not marketable.

Some investment instruments like preference shares and debentures are marketable, but there are no buyers in many cases and hence their liquidity is negligible. Equity shares of companies listed on stock exchanges are easily marketable through the stock exchanges.

An investor generally prefers liquidity for his investments, safety of his funds, a good return with minimum risk or minimization of risk and maximization of return.

An investor invests in the avenues after studying the merits and demerits of the investments. The types of investments are as:

1. Shares and debentures.
2. Government funds
3. Money market instruments
4. Public deposits
5. Bank deposits
6. Post office savings
7. HDFC schemes/Housing bank schemes

8. Mutual Fund Schemes
9. Life Insurance Schemes
10. Public provident fund
11. Gold-silver
12. Real estates

NON-MARKETABLE FINANCIAL ASSET

The financial instruments which are not transferable or saleable are known as non-marketable financial assets. The investors can invest in these instruments but they cannot transfer or sell the instruments.

A good portion of the financial assets of individual is held in the form of non-marketable financial assets like bank deposits, post office deposits, company deposits, and provident fund deposits. A distinguishing feature of these assets is that they represent personal transactions between the investor and the issuer. For example, when you open a savings bank account at a bank you deal with the bank personally. In contrast when you buy equity shares in the stock market you do not know who the seller is and you do not care. The important non-marketable financial assets held by investors are briefly described below.

1. Post office saving schemes
2. Public provident fund
3. Deposit with banks
4. Life insurance policy

1. Post Office Saving Schemes

The main financial services offered by the Department of Posts are the Post Office Savings Bank. It is the largest and oldest banking service institution in the country. The Department of Posts operates the Post Office Savings Scheme function on behalf of the Ministry of Finance, Government of India. Under this scheme, more than 20.50 crores savings account are operated. These accounts are operated through more than 1,54,000 post offices across the country.

The Post offices provide a number of savings schemes like the Savings Account Schemes, Recurring Deposit Schemes, Time Deposit Schemes, Public Provident Fund Schemes, Monthly Income Schemes, National Savings Certificates, Kisan Vikas Patras, and Senior Citizens, and Savings Scheme.

2. Public Provident Fund

PPF is a 30-year-old statutory scheme of the Central Government started with the objective of providing old age income security to the unorganized sector workers and self-employed persons. Presently, there are nearly 30 lakh PPF accountholders in India across banks and post offices.

3. Bank Deposits

Commercial and cooperative banks accept deposits from public in the form of current account which bears no interest, savings accounts which bear interest varying from 4.5% to 5.5% per annum, and fixed deposits of varying maturities.

What's the difference between savings and investment? The simple definition is savings have very little risk with low limited returns, on the other hand, investments provide the opportunity for higher returns by managing risk.

By savings in the banks, you may earn interest and you feel good and secured as you watch your money grows overtime. But hang on, if you factor in inflation you realise that you actually have a negative growth.

Alternatively, investment may provide income and capital gains with proper management of the risk involved in any form of investment. Investment comes in all sort of categories of investment assets such as Money market, Equity, Bonds, Derivatives, Unit Trust, etc.

There are two types of returns that can be derived from investments that is income and capital gains. While income is derived from your investment in the form of rental or dividends, you get capital gains from selling the investment asset for a profit.

MONEY MARKET INSTRUMENTS

By convention, the term “money market” refers to the market for short-term requirement and deployment of funds. Money market instruments are those instruments, which have a maturity period of less than one year. The most active part of the money market is the market for overnight and term money between banks and institutions (called call money) and the market for repo transactions. The former is in the form of loans and the latter are sale and buyback agreements – both are obviously not traded. The main traded instruments are commercial papers (CPs), certificates of deposit (CDs) and Treasury Bills (T Bills). All of these are discounted instruments, i.e., they are issued at a discount to theirmaturity value and the difference between the issuing price and the maturity/face value is the implicit interest. These are also completely unsecured instruments. One of the important features of money market instruments is their high liquidity and tradability. A key reason for this is that these instrumentsare transferred by endorsement and delivery and there is no stamp duty or any other transfer fee leviedwhen the instrument changes hands. Another important feature is that there is no tax deducted at sourcefrom the interest component. A brief description of these instruments is as follows:

Commercial Paper (CP)

These are issued by corporate entities in denominations of 2.5 mn and usually have a maturity of90 days. CPs can also be issued for maturity periods of 180 and one year but the most active market is for 90 day CPs.

Two key regulations govern the issuance of CPs. Firstly, CPs have to be compulsorily rated by a recognized credit rating agency and only those companies can issue CPs which have a short-term ratingof at least P1. Secondly, funds raised through CPs do not represent fresh borrowings for the corporate issuer but merely substitute a part of the banking limits available to it. Hence, a company issues CPs
almost always to save on interest costs, i.e., it will issue CPs only when the environment is such that CPissuance will be at rates lower than the rate at which it borrows money from its banking consortium.

Certificates of Deposit (CD)

These are issued by banks in denominations of 0.5 mn and have maturity ranging from 30 days to 3 years. Banks are allowed to issue CDs with a maturity of less than one year while financialinstitutions are allowed to issue CDs with a maturity of at least one year. Usually, this means 366 day CDs. The market is most active for the one year maturity bracket, while longer dated securities are notmuch in demand. One of the main reasons for an active market in CDs is that their issuance does not attract reserve requirements since they are obligations issued by a bank.

Treasury Bills (T Bills)

These are issued by the Reserve Bank of India on behalf of the Government of India and are thusactually a class of Government Securities. At present, T Bills are issued in maturity of 14 days, 91 daysand 364 days. The RBI has announced its intention to start issuing 182 day T Bills shortly. The minimumdenomination can be as low as ` 100, but in practice most of the bids are large bids from institutional investors who are allotted T Bills in dematerialized form. RBI holds auctions for 14 and 364 days T Bills on a fortnightly basis and for 91 days T Bills on a weekly basis. There is a notified value of bills available for the auction of 91 days T Bills which is announced 2 days prior to the auction. There is no specifiedamount for the auction of 14 and 364 days T Bills. The result is that at any given point of time, it is possible to buy T Bills to tailor one’s investment requirements.

Potential investors have to put in competitive bids at the specified times. These bids are on a price/ interest rate basis. The auction is conducted on a French auction basis, i.e., all bidders above the cut-offat the interest rate/price which they bid while the bidders at the clearing/cut-off price/rate get *pro rata* allotment at the cut-off price/rate. The cut-off is determined by the RBI depending on the amount beingauctioned, the bidding pattern, etc. By and large, the cut-off is market determined although sometimes the RBI utilizes its discretion and decides on a cut-off level which results in a partially successful auction with the balance amount devolving on it. This is done by the RBI to check undue volatility in the interest rates.

Non-competitive bids are also allowed in auctions (only from specified entities like State Governments and their undertakings and statutory bodies) wherein the bidder is allotted T Bills at the cut-off price.

Apart from the above money market instruments, certain other short-term instruments are also in vogue with investors. These include short-term corporate debentures, Bills of exchange and promissorynotes.

Like CPs, short-term debentures are issued by corporate entities. However, unlike CPs, they represent additional funding for the corporate, i.e., the funds borrowed by issuing short term debentures are over and above the funds available to the corporate from its consortium bankers. Normally, debenture issuance attracts stamp duty; but issuers get around this by issuing only a letter of allotment (LoA) with the promise of issuing a formal debenture letter. However, the debenture is never issued and the LoA itself is redeemed on maturity. These LoAs are freely tradable but transfers attract stamp duty.

Bills of exchange are promissory notes issued for commercial transactions involving exchange ofgoods and services. These bills form a part of a company's banking limits and are discounted by the banks. Banks in turn rediscount bills with each other.

Gilt-edged Securities

Gilts are bonds issued by certain national governments. The term is of British origin, and originally referred to the debt securities issued by the Bank of England, which had a gilt (or gilded) edge. Hence,they are called gilt-edged securities, or gilts for short. The term is also sometimes used in Ireland and
some British Commonwealth countries, South Africa and India. When a reference is made to gilts, whatis generally meant is British gilts unless otherwise specified. The description below applies to the UK gilt market. The data reveal that about two-thirds of all gilts are held by insurance companies and pension funds. During 2009, large quantities of gilts were created and purchased by the Bank of England underits policy of quantitative easing.

The term "Gilt Account" is also a term used by the Reserve Bank of India to refer to a constituentaccount maintained by a custodian bank for maintenance and servicing of dematerialized Government Securities owned by a retail customer.

Conventional Gilts

These are the simplest form of UK government bond and make up the largest share of UK government debt. A conventional gilt is a bond issued by the UK government which pays the holder a fixed cash payment (or coupon) every six months until maturity, at which point the holder receives their final coupon payment and the return of the principal.

Coupon Rate

Conventional gilts are denoted by their coupon rate and maturity year, e.g., 4¼% Treasury Gilt 2055. The coupon paid on the gilt typically reflects the market rate of interest at the time of issue of thegilt, and indicates the cash payment per £100 that the holder will receive each year in two semi-annualpayments.

Gilt Names

Historically, gilt names referred to their purpose of issuance, or signified how a stock had been created, such as 10¼% Conversion Stock 1999. In more recent times, gilts have been generally named Treasury Stocks. From 2005-2006 onwards, all new issues of gilts are being called Treasury Gilts.

BONDS OR FIXED SECURITIES

What Does Bond Mean?

A debt investment in which an investor loans money to an entity (corporate or governmental) that borrows the funds for a defined period of time at a fixed interest rate. Bonds are used by companies, municipalities, states and US and foreign governments to finance a variety of projects and activities.

Bonds are commonly referred to as fixed-income securities and are one of the three main asset classes, along with stocks and cash equivalents.

Bond

The indebted entity (issuer) issues a bond that states the interest rate (coupon) that will be paid and when the loaned funds (bond principal) are to be returned (maturity date). Interest on bonds is usually paid every six months (semi-annually). The main categories of bonds are corporate bonds, municipal bonds, and US Treasury bonds, notes and bills, which are collectively referred to as simply "Treasuries".

Two features of a bond-credit quality and durations are the principal determinants of a bond's interest rate. Bond maturities range from a 90-day Treasury Bill to a 30-year government bond. Corporate and municipals are typically in the three to 10-year range.

Definition

A debt instrument issued for a period of more than one year with the purpose of raising capital by borrowing. The Federal government, states, cities, corporations, and many other types of institutions sell bonds. Generally, a bond is a promise to repay the principal along with interest (coupons) on a specified date (maturity). Some bonds do not pay interest, but all bonds require a repayment of principal. When an investor buys a bond, he/she becomes a creditor of the issuer. However, the buyer does notgain any kind of ownership rights to the issuer, unlike in the case of equities. On the hand, a bond holder has a greater claim on an issuer's income than a shareholder in the case of financial distress (this is true for all creditors). Bonds are often divided into different categories based on tax status, credit quality, issuer type, maturity and secured/unsecured (and there are several other ways to classify bonds as well). The US Treasury bonds are generally considered the safest unsecured bonds, since the possibility of the Treasury defaulting on payments is almost zero. The yield from a bond is made up of three components: coupon interest, capital gains and interest on interest (if a bond pays no coupon interest, the only yield will be capital gains). A bond might be sold at above or below par (the amount paid out at maturity), but the market price will approach par value as the bond approaches maturity. A riskier bond has to provide a higher payout to compensate for that additional risk. Some bonds are tax-exempt, and these are typically issued by municipal, county or state governments, whose interest payments are not subject to federal income tax, and sometimes also state or local income tax.

Buying Bonds: Advantages and Disadvantages

Bonds don't enjoy the same allure as stocks, but high quality bonds should be an essential part of your financial plan. Bonds promise a steady income stream, typically at a fixed coupon rate (interest rate).

Advantages of Investing in Bonds

- Bonds are predictable. You know how much interest you can expect to receive, how often you'll receive it, and when your principal (the bond's face value) will be repaid (maturity date).
- Bonds are more steady than stocks (which can fluctuate wildly short-term). Nervous investors usually sleep better by buying bonds instead of equity investments.
- People on a fixed income and/or in retirement will receive a predictable amount of regular income from bonds.
- The interest rates paid by bonds typically exceed those paid by banks on savings accounts, especially short-term bonds.

Disadvantages of Bonds

- Companies and municipalities can and do go bankrupt, and if they do, your bonds will lose value and possibly even become worthless.
- Long-term bonds will have your money tied up in low yielding bonds should interest rates

go up.

- Unlike stocks, bonds don't offer the possibility of high long-term returns. Younger investors and those with several years to go until retirement would be better served by limiting their bond purchases and opting for equity buys instead.

Government Securities Market (G-Sec Market): It consists of Central and State Government securities. It means that, loans are being taken by the Central and State Government. It is also the most dominant category in the India debt market.

Bond Market: It consists of Financial Institutions bonds, Corporate bonds and debentures and Public Sector Units bonds. These bonds are issued to meet financial requirements at a fixed cost and hence remove uncertainty in financial costs.

Advantages:

- The biggest advantage of investing in Indian debt market is its assured returns. The returns that the market offer is almost risk-free (though there is always certain amount of risks,
- On the other hand, there are certain amounts of risks in the corporate, FI and PSU debt instruments. However, investors can take help from the credit rating agencies which rate those debt instruments. The interest in the instruments may vary depending upon the ratings.
- Another advantage of investing in Indian debt market is its high liquidity. Banks offer easy loans to the investors against government securities.

Disadvantages:

- As there are several advantages of investing in Indian debt market, there are certain disadvantages as well.
- As the returns here are risk-free, those are not as high as the equities market at the same time. So, at one hand you are getting assured returns, but on the other hand, you are getting less return at the same time.
- Retail participation is also very less here, though increased recently. There are also some issues of liquidity and price discovery as the retail debt market is not yet quite well developed.

INVESTMENT IN EQUITY MARKET

What are the advantages and disadvantages in investing in the stock market?

This is a common question among investors. Stocks and bonds differ dramatically in their structures, payouts, returns and risks. In order to answer this question, we need to go through a brief description of both stocks and bonds.

A bond is a form of debt with which you are the lender instead of the borrower. Bonds are contractual loans made between investors and institutions that, in return for financing, will pay a premium for borrowing, known as a coupon. Additionally, the bond's face value is returned to the investor at maturity. The guarantee of payback and all coupon payments relies solely on the ability of the borrower to generate enough cash flow to repay bondholders.

Stocks are a form of ownership; they represent participation in a company's growth. Generally, investors are given no promises about returns of the initial investment. In fact, the profitability of the investment depends almost entirely upon rising stock price, which, at the most fundamental level, relates directly to the performance and growth (increasing profits) of the company.

So, this leads to the original question: which security is better? The answer is neither. Stocks and bonds both have their pros and cons depending on what you are looking for. For example, risk-averse investors looking for safety of capital and who prefer a known periodic payment structure (i.e., coupon payments) for a limited timeframe would be better off investing in bonds. On the other hand, investors who are willing to take on greater risks than bondholders and who would prefer the benefit of having partial ownership in a company and the unlimited potential of a rising stock price would be better off investing in stocks.

However, the disadvantage of stocks versus bonds is that stocks are not guaranteed to return anything to the investor while the coupon payments and principal of bonds are. Thus, the possibility for high returns is greater with stocks but so is the possibility of losing money.

For most investors, a combination of stocks and bonds is the best situation. By diversifying your investments and putting some money into both stocks and bonds you ensure some safety while leaving some opportunity for above-average returns in your stock investments.

Advantages:

13. You own your own business with literally do nothing.
14. Flexible holding position, which you can liquidate it anytime you want, no string attach.
15. Unlike other business, you need a team. But here, you can work yourself, and from home!

Disadvantages:

1. Very steep learning curve in the beginning.
2. It is not that easy to control your emotion.
3. You can end up broker if you do things wrong.

MUTUAL FUND

Mutual funds are money-managing institutions set up to professionally invest the money pooled in from the public. These schemes are managed by Asset Management Companies (AMCs), which are sponsored by different financial institutions or companies.

Mutual Fund is an ideal investment vehicle where a number of investors come together to pool their money with common investment goal. Each Mutual Fund with different type of schemes is managed by respective Asset Management Company (AMC). An investor can invest his money in one or more schemes of Mutual Fund according to his choice and becomes the unitholder of the scheme. The invested money in a particular scheme of a Mutual Fund is then invested by fund manager in different types of suitable stock and securities, bonds and money market instruments. Each Mutual Fund is managed by qualified professional man, who use this money to create a portfolio which includes stock and shares, bonds, gilt, money market instruments or combination of all. Thus Mutual Fund will diversify your portfolio over a variety of investment vehicles. Mutual Fund offers an investor to invest even a small amount of money.

Mutual Funds schemes are managed by respective Asset Management Companies sponsored by financial institutions, banks, private companies or international firms. The biggest Indian AMC is UTI while Alliance, Franklin Templeton, etc., are international AMCs.

Mutual Funds offers several benefits to an investor such as potential return, liquidity, transparency, income growth, good post-tax return and reasonable safety. There are number of options available for an investor offered by a mutual fund.

Before investing in a Mutual Fund an investor must identify his needs and preferences. While selecting a Mutual Fund's schemes he should consider the effect of inflation rate, diversification of investment, the time period of investment and the risk factors. There are various type of risk factors as:

(a) Market Risk
(b) Credit Risk
(c) Interest Rate Risk
(d) Inflation Risk
(e) Political Environment

CRISIL's composite performance ranking (CPR) measures the performance for each of the open- ended scheme of Mutual Fund. There are four parameters considered to measure the performance of a mutual fund such as Risk-adjusted returns of the scheme's NAV, Diversification of Portfolio, Liquidity and Asset Size.

LIFE INSURANCE

Life insurance is a contract between the policyholder and the insurer, where the insurer promises to pay a designated beneficiary a sum of money (the "benefits") upon the death of the insured person. Depending on the contract, other events such as terminal illness or critical illness may also trigger payment. In return, the policyholder agrees to pay a stipulated amount (the "premium") at regular intervals or in lump sum. In some countries, death expenses such as funerals are included in the premium; however, in the United States the predominant form simply specifies a lump sum to be paid on the insured's demise.

The value for the policy owner is the 'peace of mind' in knowing that the death of the insured person will not result in financial hardship.

Life policies are legal contracts and the terms of the contract describe the limitations of the insured events. Specific exclusions are often written into the contract to limit the liability of the insurer; common examples are claims relating to suicide, fraud, war, riot and civil commotion.

Life-based contracts tend to fall into two major categories:

- Protection policies – designed to provide a benefit in the event of specified event, typically a lump sum payment. A common form of this design is term insurance.
- Investment policies – where the main objective is to facilitate the growth of capital by regular or single premiums.

Life insurance has the highest penetration levels amongst investment options with 44 per cent, followed by Bank Fixed Deposits which has 35 per cent votes. Gold (33%) and Property (23%) are the other favourites among Indians. The current financial turmoil makes it a tough case for equity markets.

INVESTMENT IN REAL ESTATE

The real estate sector in India is of great importance. According to the report of the Technical Group on Estimation of Housing Shortage, an estimated shortage of 26.53 million houses during the Eleventh Five Year Plan (2007-12) provides a big investment

According to a report 'Emerging trends in Real Estate in Asia-Pacific 2011', released by PricewaterhouseCoopers (PwC) and Urban Land Institute (ULI), India is the most viable investment destination in real estate. The report, which provides an outlook on Asia-Pacific real estate investment and development trends, points out that India, in particular Mumbai and Delhi, are good real estate investment options for 2011. Residential properties maintain their growth momentum and hence are viewed as more promising than other sectors. ULI is a global non-profit education and research institute.

Further, real estate companies are coming up with various residential and commercial projects to fulfil the demand for residential and office properties in Tier-II and Tier-III cities. For instance, Ansal Properties has several residential projects in cities such as Jodhpur, Ajmer, Jaipur, Panipat, Kundli and Agra. Omaxe has also planned around 40 residential and integrated township projects in Tier-II and Tier-III cities, majority of them being in Uttar Pradesh, Punjab, Madhya Pradesh, Rajasthan and Haryana. The growth in real estate in Tier-II and Tier-III cities is mainly due to increase in demand for organized realty and availability of land at affordable prices in these cities.

Real estate is a legal term (in some jurisdictions, such as the United Kingdom, Canada, Australia, USA, Dubai, Trinidad and Tobago and The Bahamas) that encompasses land along with improvements to the land, such as buildings, fences, wells and other site improvements that are fixed in location— immovable. Real estate law is the body of regulations and legal codes which pertain to such matters under a particular jurisdiction and include things such as commercial and residential real property transactions. Real estate is often considered synonymous with real property (sometimes called realty), in contrast with personal property (sometimes called chattel or personality under chattel law or personal property law).

However, in some situations the term "real estate" refers to the land and fixtures together, as distinguished from "real property", referring to ownership of land and appurtenances, including anything of a permanent nature such as structures, trees, minerals, and the interest, benefits, and inherent rights thereof. Real property is typically considered to be immovable property. The terms real estate and real property are used primarily in common law, while civil law jurisdictions refer instead to immovable property.

INVESTMENT IN PRECIOUS METALS

A precious metal is a rare, naturally occurring metallic chemical element of high economic value. Chemically, the precious metals are less reactive than most elements, have high lustre, are softer or more ductile, and have higher melting points than other metals. Historically, precious metals were important as currency, but are now regarded mainly as investment and industrial commodities. Gold, silver, platinum, and palladium each have an ISO 4217 currency code.

The best-known precious metals are the coinage metals gold and silver. While both have industrial uses, they are better known for their uses in art, jewellery and coinage. Other precious metals include the platinum group metals: ruthenium, rhodium, palladium, osmium, iridium, and platinum, of which platinum is the most widely traded. Radioactive polonium, radium, actinium and protactinium, are not considered precious due to the health risk they pose.

Why Invest in Precious Metals?

In the past, people have invested in gold or silver as a method for storing value when a currency was losing its value. But today, our currency is no longer backed by gold per se. It is backed by the gross domestic production of the nation. Now there are many other reasons people have for investing in these precious metals. For the last several years, the consumption of gold, silver, platinum and palladium has far exceeded its production. This is coupled by the fact that the market price of these precious metals has been kept relatively down by the selling of gold reserves by central banks. In addition to this,rich foreign investors from developing countries have been increasingly looking for an investment to store away their personal wealth. They are moving out of their governments, which are often in the hands of corrupt politicians. It would take a global recession to slow the demand for gold and other such precious metals. Precious metals have long been looked to as the repositories of absolute value – not the relative value of paper currency.

When most people think of investing in gold and precious metals, they think of bullion (bars and wafers). Although many people do invest in bullion, there are investments in many different forms. Precious metal investments can be made in jewellery, coins, bullion, futures, options, mining stocks, or mutual funds. In this sense, they have tremendous liquidity and can be bought and sold without problems. Platinum and palladium, however, are less liquid than gold and silver. Each of the above types of precious metal investments is easy to get into and to get out of.

For these and similar other reasons, many investor’s allot a portion of their portfolios to precious metal assets. Like other investments, the gold/silver market prices go through tremendous cycles. Prices moved from about $140 an ounce in early 1977 to over $887 an ounce in early 1980. When confidence in other assets causes their values to plummet, precious metals often do well. But as a result, investing in gold has been especially speculative, as you can see.