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Macroeconomics Determinations of Gold Price in United States

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ABSTRACT

Nowadays, gold prices have been volatile, and the wealth of gold investors depend on the movement of gold prices. The purpose of this study is to examine the relationship between gold prices, crude oil prices, inflation rate, real interest rate and stock prices in United States. This study uses monthly data covering the period ranging from January 1990 to August 2018. The Johansen and Juselius (JJ) Cointegration test and Vector Error Correction Model (VECM) are conducted in this study. The result shows that there is a long-run relationship among gold prices, crude oil prices, inflation rate, real interest rate and stock prices. The results show that inflation rate and crude oil prices are significance and positively related to gold prices, while stock prices and real interest rate are negatively affecting gold prices. There are three unidirectional Granger causality and one bidirectional Granger causality in the short run. Only inflation rate Granger cause gold price, which means that inflation rate directly affects the gold prices. This study allows community such as central bank, government, financial institution, economist, investor and policy makers in manipulating and controlling the movement of the gold prices so that they have a better decision making to diversify their risks.

Key Words: Crude Oil Prices, Gold Prices, Vector Error Correction Model (VECM), Granger Causality

INTRODUCTION

According to Andrew (2018), gold is one of the oldest means of exchange and can be considered as one of the precious metal. In fact, gold is both a commodity and a currency because of its intrinsic value. The Classical Gold Standard was the first international monetary system developed. According to Sukri, Zain and Abidin (2015), since thousands of years ago, many people have been fascinated by gold. It is because gold is a light, generally accepted and durable metal. Based on Hashim, Ramlan, Razali and Nordin (2017), many years before, man y people declared that gold was a symbol of prosperity and also wealth. Before fiat money, gold was used as a currency and now it is used as an investment both in computer and jewelry. Based on Eric (2012), most of the businesses are likely to make the gold into jewelry to attract more consumers. Hence, the jewelry is made by consuming around 78% of gold and it is the main use of gold in different cultures.

Gold also helps to offset the big losses that suffer by investors such as the risk of asset depreciation or investment losses, and thus it is also known as a hedging tool. The investors will use gold as an asset to hedge against the highest risk when the economy is unstable or cannot be expected. As a result, gold has become a possible financial staple. Basically, investors invest in gold mainly to hedge against inflation and political turmoil in their investments because gold acts as a commodity which can reduce the portfolio risk. It means that when the rate of inflation increases, then the gold price will also rise. Gold is also classified as a financial asset, in addition regarded as a commodity. That means that gold is a safe storage as it is a store of wealth. Today, gold has attracted many of the investors to keep or invest in it as future assets investment. According to the study by Wang (2013), the future value of gold is more liquid compare to paper money or stock as gold is one of the hedging tools. On the other hand, in year 2018, there was a trade war between China and United States (US). According to Nick (2018), US want to raise 10% to 25%, which is $200 billion of the tariffs on Chinese goods because Washington has increased its control over the increasingly fierce US-China trade war. In response to these ‘rumors’ China said that they would take appropriate measures. Basically, the investors will seek for the gold to reduce their risk (Nick, 2018). However, based on Figure 1, we can clearly see that the gold price decreased to USD122 per troy ounce from March 2018 to August 2018. It means that gold remain weak, pressed by a weak Chinese Yuan and a strong US dollar. The expectations of higher US interest rates continue with a third 0.25% increase in this year which has already reflected in September and the fourth in December. Thus, the relationship between gold prices and other assets prices assumes that the investors’ predictions will towards the unforeseen circumstances. It is