

Triple Top

Dennis Gartman on CNBC earlier in the week said this would be the most boring FOMC statement from the Federal Reserve this year. He was correct.

The Fed released a status quo policy announcement on Wednesday that was a stark difference from the fireworks created by their prior September statement and press conference. The Fed opted to keep their asset purchases via Quantitative Easing unchanged at \$85 billion a month to be split between US Treasuries and Mortgage Backed Securities. The new consensus for the inevitable Fed taper has been pushed back to March of 2014, and with that the price of gold did a triple top at 1,360 USD per ounce, and then headed lower to finish the week, as the metals market once again looks to be under pressure.

Jon Hilsenrath, economics editor for the Wall Street Journal best summed up the uncertainty about when we will see the Fed begin to taper; “it’s anyone’s best guess.” And this relates to understanding how the US central bank operates and makes their decision. Every policy announcement or statement, and thus change in policy direction is decided upon by quantifying the most recent economic data. So as Hilsenrath explains, predicting when the Fed will taper is the equivalent to forecasting GDP, because without knowing how the economy will perform, it’s impossible to set a timeline for the Fed’s decision-making process. Furthermore, with the manufactured uncertainty and headwinds to economic growth created by the US government in Q4 of 2013, forecasts become even less reliable.

What we have seen in the markets though, in reaction to the US Federal Reserve and the announcement of continued easy money policies, is similar to what we are witnessing in the overall economy, and that is that they seem directionless. When 2012 seemed like a mediocre year for economic growth, and analysts were looking for the pickup in 2013—

that too did not exactly come to fruition. Instead, what prevailed was more of the same tepid growth levels restrained by uncertainty relating to central bank and government policy.

Without trying to forecast GDP, it seems inevitable the Fed will begin to taper asset purchases sometime in 2014, which is encompassed in the price of gold. And there are two strong supporting pieces of evidence for why this taper will come. Firstly, each US Treasury auction in the second half of this year has seen the Treasury department cut the number of bonds they are issuing to the market. Second, sequester budget cuts, and then constrained budget negotiations going into the New Year force austerity measures on US government spending. With a diminished supply of Treasuries going to market, nor the same level required to finance their deficit, the Fed’s involvement in the market thus becomes limited. Without the supply of newly issued government debt, the Fed does not, and will not need to be as an active of player.

Looking at the price of gold then heading into the New Year keeps with the short term bearish outlook. The problems with the US government debt aside, gold has become out of favour; therefore, excess selling in the market will keep downward pressure on prices. Moreover, even as the market is in search of a bottom, there is still reason to see higher prices in the years ahead. The US government’s inability to control their debt load is what keeps the long-term outlook bullish. We can look for strong economic growth to allow the issuer of the world’s reserve currency to manage their debt load, but likely it will be inflationary policy which attempts to keep their debt intact, and that ultimately will drive the price of gold to new record high prices.

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