

## The Inevitable Taper Part II

*"The markets can remain rational longer than you can remain solvent."*

-John Maynard Keynes

It might have gone against the conventional wisdom to see the markets trade higher on the basis that the US Federal Reserve will begin, come January, to be less accommodative to the US economy, but it's not exactly as if the markets have had a perfectly rational last few years. Amidst one of the shakiest recoveries from the greatest recession to plague the US economy since the Great Depression, we continue to see equity markets trade higher as all the disbelievers missed out on the seventh greatest annualized gain in the American stock markets since World War II. No question, it was the US Federal Reserve's influence on long term borrowing rates that bestowed confidence in American consumers, and nonetheless fueled this American recovery, but as the Fed begins to adapt their stimulus measures to adequately reflect the necessities of this continued recovery, we can be certain the party's not over yet.

Ben Bernanke, in his final press conference as the Chairman of the US Federal Reserve, assured investors of one thing, and that was that the Fed will continue to adapt to the needs of the economy. And just as easily as they could trim asset purchases by 10 billion a month equally split between Treasury bonds and mortgage back securities, they could increase by 10 billion as well. But as we at Border Gold have argued in past newsletters, the taper of the Fed's asset purchases was very much an inevitable occurrence; moreover, it is absolutely not to be confused with the end of an era of easy money policies in the months and years to come.

And as the easy money policies will continue the biggest influence on the market will be near zero short term interest rates, controlled by the Federal Funds Rate. Offered in the form

of forward guidance, Bernanke made clear in his policy statement that rates will remain low "well past the time that the unemployment rate declines below 6-1/2 percent." And that low of emergency level interest rates will be the fuel to the fire for the markets. It makes sense for the stock markets to be able to trade higher, almost in relief to the fact the world's largest economy is no longer so desperately in need of such extraordinary stimulus. But it is the caveat that the highly accommodative economic environment will remain in place.

As the Berkley Economist Barry Eichengreen phrases it, a reduction "by \$10bn a month is best dismissed as a taper in a teapot... \$10bn of monthly security purchases are a drop in the bucket for a central bank with a \$4tn balance sheet." And in fact, by Bernanke beginning the taper, he began the very seamless hand off to Janet Yellen to fulfill the role of an accommodative central banker. This is as the markets can now digest the milestone that a measure once dubbed "QE Infinity" has the possibility of coming to an end.

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### A Note on Gold:

Following what was a supposed short covering rally with the rest of the market given the Fed's decision to taper, gold immediately sold off heading for that June low of 1180 US/oz. Thursdays close on the Comex, below 1200 US/oz. was the yellow metals lowest in three years' time. From a technical stand 1180 stands out as an important number, but as this market faces tax loss selling pressure going into yearend precious metal markets are giving an indication that they are in the process of forming a bottom in Q1 of 2014.

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