

## Gold: An Insurance against Illiquidity

The renowned commodities investor Donald Coxe wrote in the Globe and Mail this week on what seems to be an original and profound thesis for gold. Where many have witnessed for years gold's role as hedge or safe haven during times of economic turmoil and financial instability, it may play a positive role in good economic times as well. From the data alone, academic research can illustrate gold's role as a safe haven since the price floated in 1971. It is an asset that exhibits close to zero correlation with US equity markets, which means there is no relation in price movements. And Don Coxe does not refute that in gold's price history. Instead, in what seems to be a welcomed idea for gold investors, it's that instead of waiting for fear to grip financial markets once again, imagine a world in which gold can rally in a positive economic environment.

Ideas like this are novel and welcomed. I think it is unfortunate that the idea of believing in gold is associated with fear mongering and awaiting an eventual economic collapse, especially during a period of repeated new highs in equity markets. But as many analysts seem to be forecasting, we could very well have just witnessed only the beginning of what will be a cyclical multiyear rally in stocks, and with that comes a recovering strength to the global economy. If Europe is able to move past their triple dip recession, they potentially have the most to gain. Being a group of economies that have stalled out for so long, and are in the process of applying needed structural changes, could pave the way for opportunity in productivity and manufacturing gains. The other key driver for Europe, which relates to a story without the United States, is that they are on aggregate the biggest importer of goods and services from China. This provides the elements

for a rebounding global economy with resurging growth from emerging markets as well.

In the US we are witnessing a renewed growth in the oil and gas sector. With that, States linked to extraction and refining stand to benefit. This sector has acted as the catalyst for economic growth in the United States; furthermore, it's truly surprising that the Obama administration is taking this long to make a decision Keystone XL pipeline. Wavering around the issue of coal production when it's a far greater polluter than the tar sands crude, illustrates how political this issue has become, and exemplifies that this is a decision without thought to sound economic policy. Without moving too far from the point though, what is evident from what we see in the US right now is that they may lead the globe out of the financial crises that roiled the world markets 5 years ago, but their position as the world economic leader will not be sustained.

Resurging economic growth, however, will lead to the inevitable rise in interest rates. The US Fed will be first, but other central banks will quickly follow. This is central to Coxe's thesis. Central banks will be forced to act to contain short term inflationary threats and increasing rates of nominal economic growth. In doing so liquidity, the very fuel to the fire that helped stock markets soar out of the 2008 downturn, will begin to dry up. Rising interest rates make the cost of borrowing more expensive and see tighter credit conditions for borrowers. As we see less liquidity in the capital markets, funds will have to go elsewhere. And perhaps, gold becomes that attractive opportunity for an inflow of capital, but perhaps it is also that insurance against decreasing liquidity.

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