These charts will tell you most likely what will happen. Yields to 1.5%, US dollar index down to 74, Yen stronger, copper down below $3/lb, Shanghai index down and gold up!

A picture is worth a thousand words!!

Chart: 10 year Treasury yield

Chart: 10 year Treasury yield versus the gold price

Chart: USD index versus the gold price

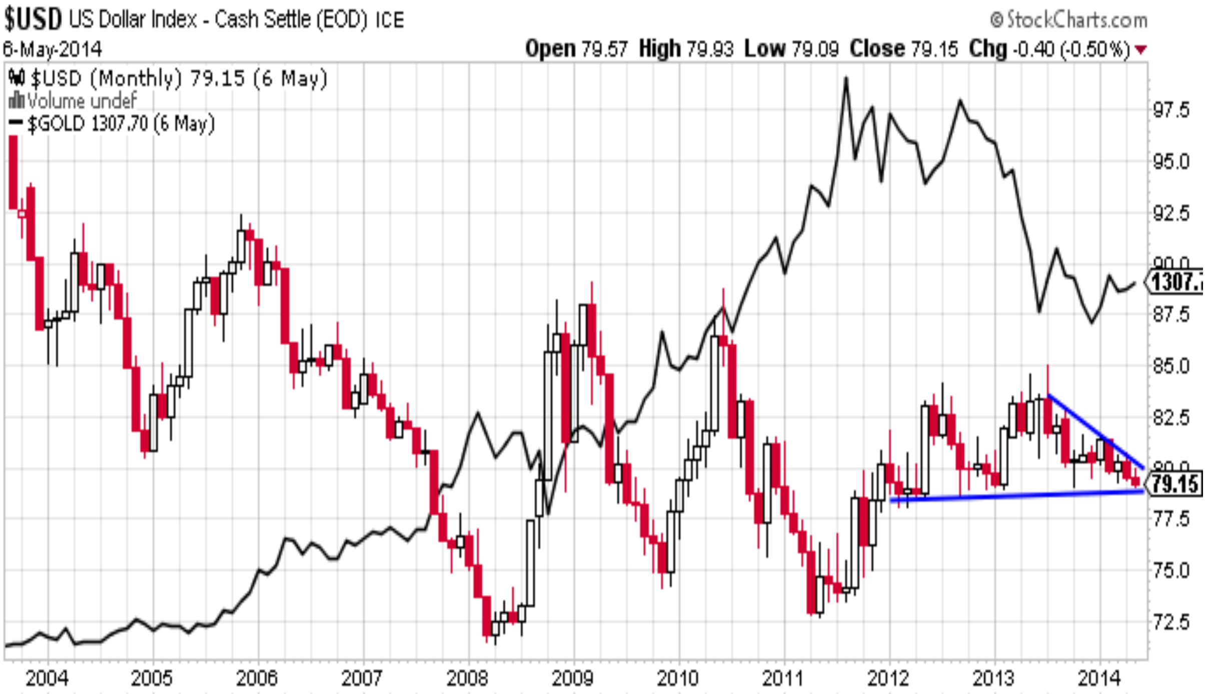


Chart: Japanese Yen versus the gold price

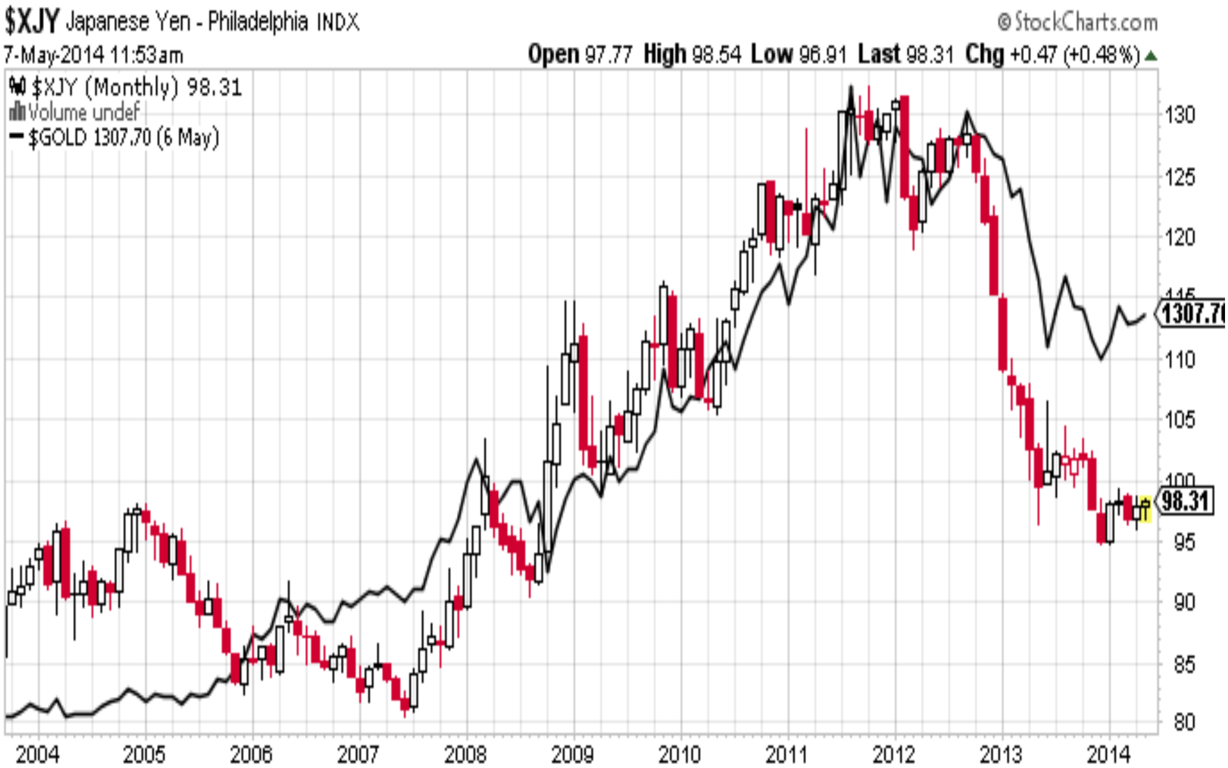


Chart: Copper price

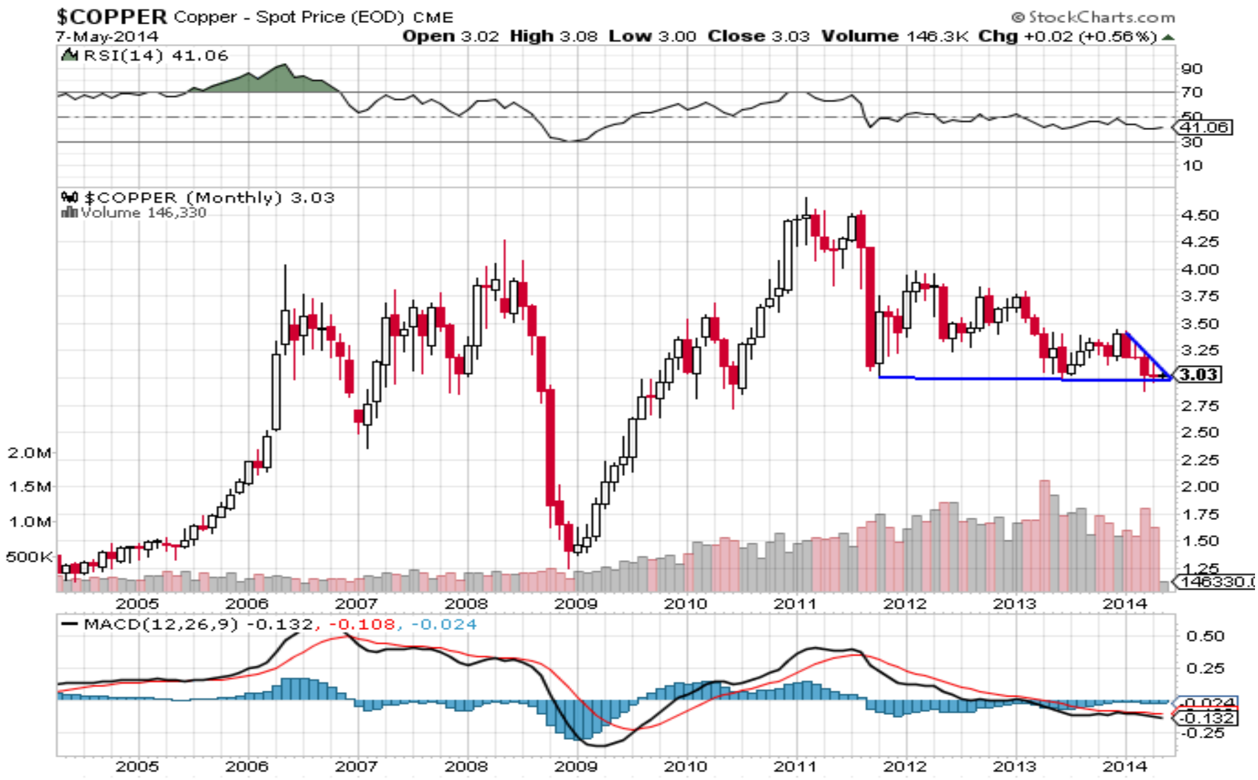


Chart: Shanghai Index

The bond market is giving the stock market angst and rightfully so! It feels like Japan in 1989

Is any stockbroker going to say, “The figures look awful and unrealistic”? Of course not because they would ruin their own income so how independent and objective is your broker? They are not, they are like lemmings, and therefore any news good or bad will be twisted so that it is “good news”. Bad news is good news and good news is good news. It is like the market only can go up. It feels more and more like the Nikkei when it was at its last legs making highs above the 38,000 level in 1989. We all know what happened afterwards.

Whilst the market is short long term treasuries the yield is likely to continue lower, due to weak economics (housing, labor participation) and a weak $, which could create a blood bath in the bond markets.

The yield on the 10-year note has become a barometer for stocks as it hovers near the bottom of this year's range. At the same time, the yield curve has been flattening; meaning yields on shorter-duration securities are getting closer to longer-term rates, which are coming down- usually a bad sign for stocks.

Zero GDP growth, manipulated birth/death model jobs figure and falling participation rate

As reasons for lower long-term rates are mentioned the zero GDP growth and the falling participation rate. First quarter gross domestic product (GDP) came in at 0.1% whilst new jobs for April came in at 288,000 though only 51,000 when one deducts the 234,000 payrolls added according to the birth-death model by the Bureau of Labor Statistics. The birth-death model,” which factors in jobs assumed to have been created by employers who are too new to have been included in the survey, and subtracts jobs from employers assumed to have failed and therefore not responded to the latest survey. It is an instrument that allows for huge manipulation of the real figures just to suit the politicians. It now appears that during the first half of 2008, when the recession was getting under way, real job losses averaged 146,000 per month. That is nearly three times the average of 49,000 jobs shown in the initial estimates including the birth-death model jobs. The lack of a gain in hourly wages and a big drop in the participation rate, people dropping out of the workforce because they get so disillusioned so much by the lack of prospects, were seen as signs of economic weakness.

A lot of bond investors are wrongly positioned expecting long-term yields to rise

"Everybody's got the same question - why are Treasury yields so low? And the answer is really simple - because everybody thought they were going to be so high," said Jeffrey Rosenberg, Black Rock chief fixed income investment strategist. "I think at the end of the day, the explanations are trying to justify a move…the simplest one is positioning matters. You can't really explain it through fundamentals." Rosenberg expects yields to move higher from current levels.

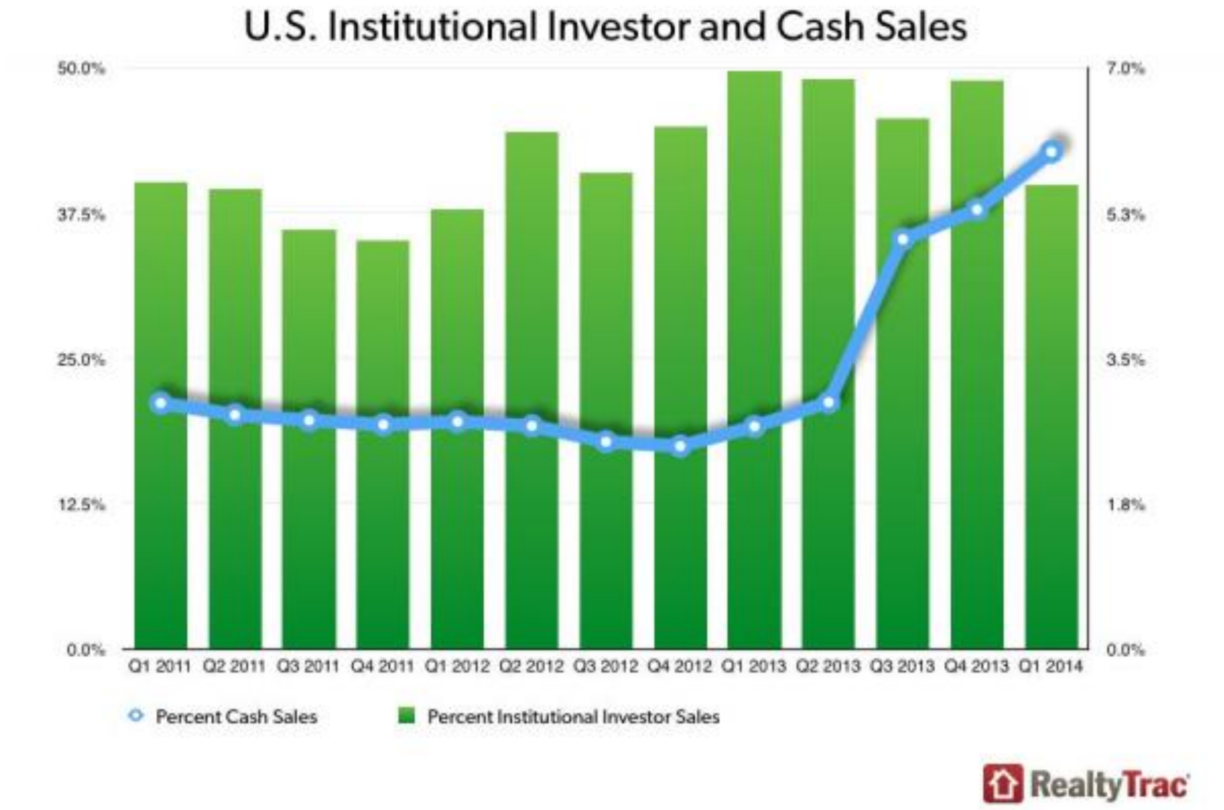
Rosenberg said he expects the 10-year yield to be about 3.25% to 3.50% by the end of the year. The 10-year yield started the year at 3%, and many money managers went short, expecting higher rates this year. But the yield has moved lower since Dec. 31 and touched the lows of the year at 2.56% on May 5.

I personally think that the low 10 year yield is partly a result of the wrong positioning of a lot of bond investors though underlying this situation and more fundamental is the very weak economy and the very weak, and potentially much more weakening, US dollar.

What is a 19-year low for homeownership and cash buys telling you?

All-cash purchases accounted for almost 43% of all sales of residential property in the first quarter of 2014, up from almost 38% in the previous quarter and 19% in the first quarter of 2013; according to data released from real-estate data firm RealtyTrac. “It’s a surprising thing for us that cash sales have stayed high for so long even though the big hedge fund investors have pulled out of the market a bit,” says Daren Blomquist, vice president at RealtyTrac. “The high percentage of cash sales reveals the soft underbelly of the housing recovery. “Who has the cash lying around to pay for a house? Only very few, it is definitely not valid for the majority of the population.

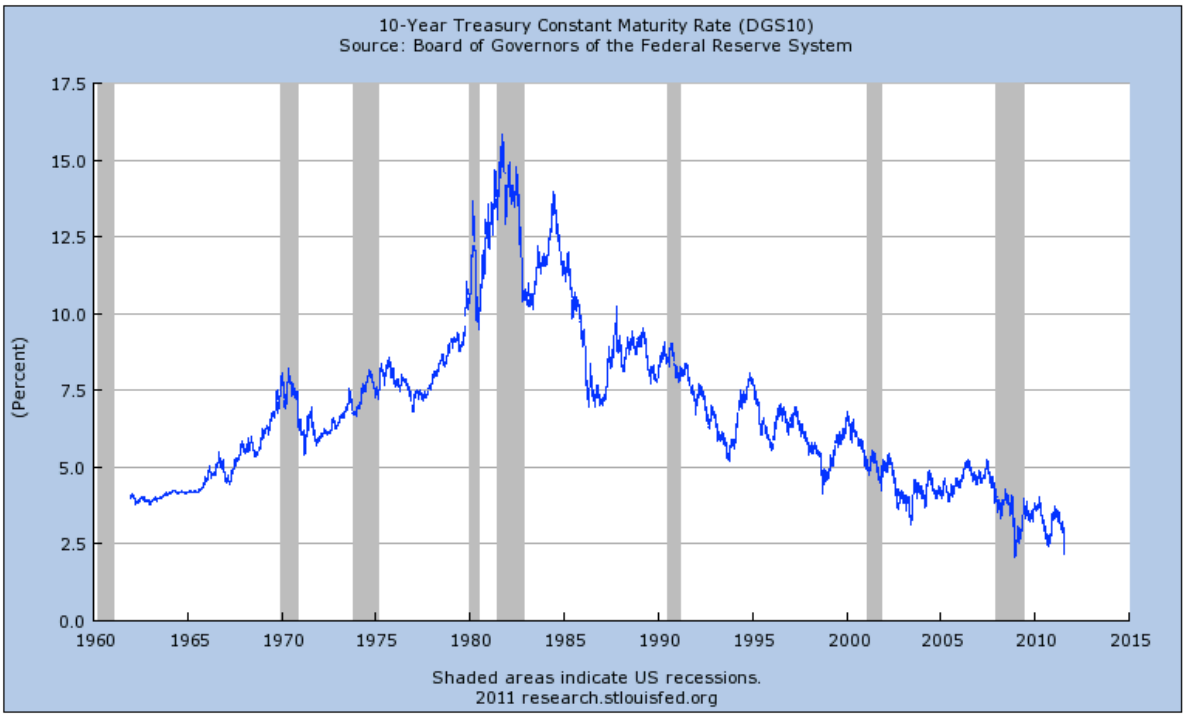
Experts say the high percentage of those paying cash won’t last much longer, though. “Cash buyers will become few and far between,” Blomquist says. So you have to wonder where the money will come from going forward to keep the market up? Moreover who does have the money to buy a home outright? Wealthy Americans and downsizing empty nesters make some of these all-cash deals, Blomquist says. Investors who are eager to make a profit by buying low and renting those properties — or flipping them — also drive up the number of all-cash deals, he adds.



Sounds like an ok home market, no!? As mentioned many times before this is a very unhealthy housing market with only the wealthy (wealthy individuals or private equity firms such as Blackstone although they are now slowly exiting the market!?) being able to buy houses whilst at the same time the middle class "wealth" is being eroded at an accelerated pace and rents being pushed to new highs because very few people can afford buying a house and thus more people are renting. Homeownership is at a 19 year low, you know why? Again because the housing prices have been artificially boosted by the purchases of thousands of homes by private equity firms. Just to remind you the health of the housing market will be reflected in the health of the economy. Housing is the most important asset for most people and a healthy housing market, not a "flipping" market, will allow middle class people to use their house as a collateral for credit with the banks allowing them to purchase goods which then in turn again boost GDP. Anyway I have just set out why it is not a healthy housing market! And on top of that people are falling left right and center out of the workforce. Consumer spending, which is equal to 2/3 of GDP, is determined for 75% by consumer confidence. Do I need to say more, low housing affordability, no outlook for jobs, which consumer confidence!

The 10-year yield, US dollar, copper and Shanghai Index charts, which are looking to break down anytime, show a lot of analogy!! A bloodbath in the making? And a lot of fund managers don't understand the mindset of a bear market!

Yes the economy is really doing well! Not! If you look at the charts, that show a lot of analogy, you see that the 10-year yield, the copper price and the US dollar could anytime break below their declining triangles. If there's a big move in the market toward lower yields, those shorts would cause a massive squeeze, driving yields even lower and at the same time creating a bloodbath worldwide. Especially because a lot of these bond funds are leveraged many times in order to get a decent return. The 10-year hit 1.39% in July, 2012. Times are changing and a lot of hedge funds don't understand the dynamics of a true bear market because they have always been used to markets only going up (like in Japan before 1989) supported by the Fed!! You think hedge funds are now having a difficult time wait and see what will happen going forward you haven't seen anything yet when everything will start to feed on itself. They, the hedge fund managers, except for a few, don't have the mindset to deal with bear markets. Look at Pimco, Bill Gross did so well for the last 10,20, 30 years because the market basically went in just one direction from 16% to 2.6% and that was up and up for the bonds.



But now times are changing and it is becoming much more difficult hence why he is underperforming and investors are withdrawing money from his funds!

Either the 10-year is too low or the S&P500 is too high, or a combination! I believe the economy is weak hence why the US dollar is, very, weak. Think what that could mean for the bond market!

Anyway if the bond market declines are really signaling what they normally are signaling, then there's a disconnect in market pricing. The broad market concern is not the level of the 10-year, it's the level of the S&P 500. If the 10-year is right, then the S&P 500 is wrong. The bond market would then be pricing in recession or a growth slowdown. As potential other reasons for the low 10 year yields have been mentioned a flight to safety due to tensions in Ukraine was one factor, and there was also a lot of talk about pension funds, locking in gains in equities and moving proceeds to the bond market. Although the latter reason makes sense, the geopolitical reasoning doesn’t because normally the US dollar would get stronger following these events, it didn’t the Euro, sterling and gold and silver strengthened. In other words if the move in the bond market were geopolitical, the US dollar would be moving higher with foreign money coming in.

Basically what one should deduct from all these different movements is that the economy is weak or that the market is expecting a deteriorating economy despite all the bullish comments on CNBC. And the weakness also shows in the weak US dollar.

The strength in the Yen indicates an astonishing weakness in the US dollar

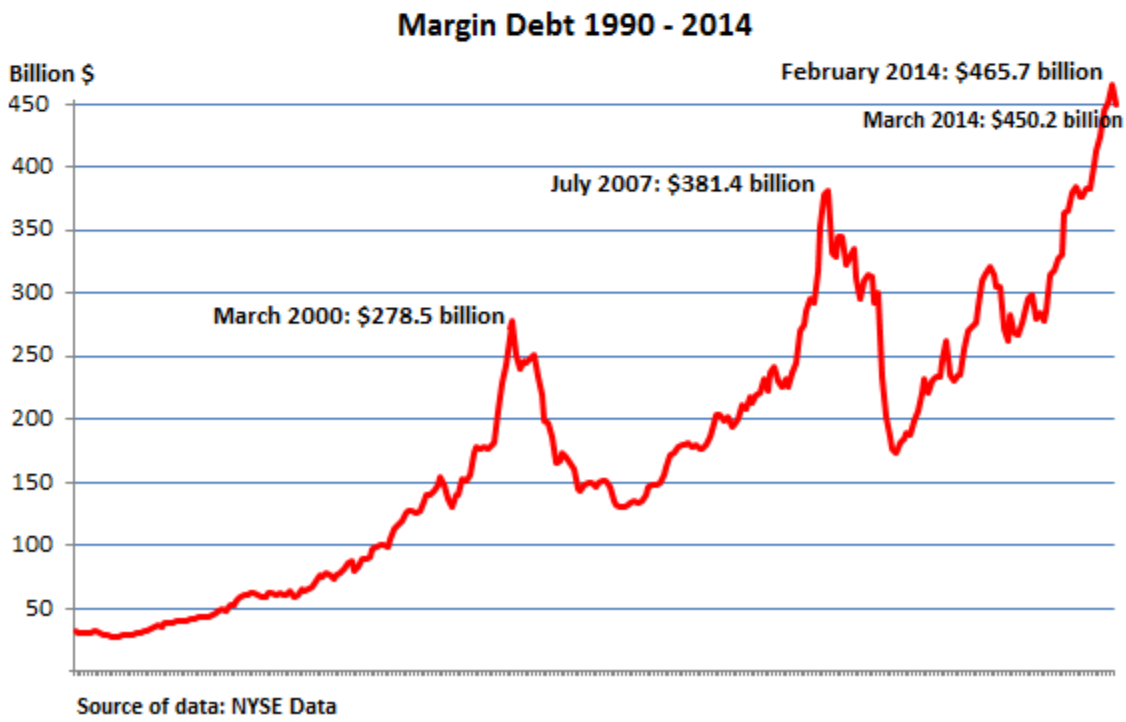
The fact that even the Yen despite all its stimulus and Abenomics is strengthening tells you how incredible weak the US dollar is!!!! The yen rose against other major currencies but especially against the US dollar, crossing the 102 level, despite the minutes of the Bank of Japan's April Monetary Policy Meeting that showed that the policy board decided to conduct money market operations so that the monetary base will increase at an annual pace of about 60-70 trillion yen.

An index monitoring the service sector in Japan moved into contraction in April, the latest PMI from Markit Economics showing a score of 46.4. That's down from 52.2 in March. It fell below the '50' level that shows contraction. And despite this all the yen recovered to 101.53 against the greenback. Wake up this is telling you something!! If the US dollar can’t stand its ground against the Yen which is being weakened continuously and with a Debt/GDP ratio of 230%+ the US dollar must be in real dire straits. And be aware that If the US dollar index falls from 79 to 74 this would represent a 6.3% fall in the $ currency versus a basket of other currencies. Kiss goodbye to possible gains for foreign bondholders re their treasury holdings.

The conclusion should be that even if the US dollar can be upheld for now sooner or later gravity will have its way with gold and silver the main beneficiaries.

Dr Copper, with its ability to predict turning points in the global economy, clearly doesn't show much upside according to its chart as is confirmed by the Shanghai index. The intricacies of housing and the falling participating rate are not particularly an indication of strength hence why falling long term interest rates are flattening the interest curve which is causing a lot of pain for bond market investors that are short. Some people are saying that investors are buying US treasuries because of liquidity reasons (a $10trn market) and the safe haven bond status and not for their return. But the next question than is "why is it then that the US dollar is so weak?"

In the end the currency is the benchmark of your wealth. Ask the Europeans who visit the US if they feel "rich". The extreme weakness in the US dollar as most blatantly expressed by an even stronger Yen which doesn't bode well for the markets. A declining currency can easily wipe out all your gains if any. Gold and silver should go through the roof but are clearly "managed" but for how much longer? Anyway for the moment it looks like gold doesn't want to fall too much below the $1,300 level. Have a good read of the charts and draw your own conclusion what you think will happen to the gold price when the 10-year yield and the US dollar drop. Put the different charts into context and don't ignore what the consequences and fall out could be if the yields keep on dropping further. In 2007/2008 a lot of bond funds were leveraged many times over in order to boost their return though when wrongly positioned this of course also works the opposite way! Just look at the following chart and try to convince yourself that this is all normal. Best.



May 8, 2014 Gijsbert Groenewegen

g.groenewegen@goldarrowpartners.com

www.groenewegenreport.com