Resource Stock Update V20 #15.3 Markets, Gold, Bonds, Deflation Oct. 16, 2014

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The recent market action has been fascinating and is proving exactly what I expected and proving what I have been saying that the market had it all wrong.

The Empire State manufacturing survey shows that business conditions in New York weakened significantly in October, giving back all of the gains seen last month. The general business conditions index in the manufacturing gauge fell 21 points in October to a reading of 6.2, compared to September’s reading of 27.5. According to consensus estimates, economists were expecting to see a modest pullback in the region’s manufacturing sector and were forecasting a reading of about 20.3.

The U.S. Census Bureau said retail sales fell 0.3% in September. According to consensus reports, economists expected retail sales between a drop of 0.1% and a rise of 0.3%.

Sept. 10th I commented that another deflation wave might be on the way, I was re-enforcing this in an update Sept 22nd and now it looks like very little doubt. The US$ might have been pushed up and Euro down as to help the European economy which had more deflationary pressure but now we see the deflation in the U.S. and else where.

CPI figures from across the EU highlight the deflation threat to the region. French CPI dropped 0.4% on month in September from +0.5% in August and Italian CPI slipped 0.4%, as in August. Spanish CPI held steady at +0.2% on month but was -0.2% on year. In the U.K., annual inflation dropped to a five-year low of 1.2% from 1.5%.

Chinese inflation dropped to an almost five-year low in September, tumbling to 1.6% on year from 2% in August and coming in below consensus of 1.7%. Factory gate prices (PPI) slumped 1.8% vs -1.2% previously. "*You got falling oil prices, falling house prices, excess capacity in the industry and an appreciating currency,*" says BNP economist Richard Iley. "*So everything is pointing to deflation getting a whole lot worse before it can get better.*"

In the U.S. CPI declined -0.04% in July and -0.17% in August, September's CPI will be released next Wednesday

You will hear the main stream harp about weak U.S. Economic data, problems in Europe etc. etc., but the real reason the equity markets have fallen so hard and fast was because they were way over bought – driven by money printing, QE

I said the US$ rose in a frenzy because hot money was pouring in but it could leave just as fast and it has been. The S&P 500 fell straight through support around 1850 with only a hiccup, a hold above it for 1 day, but has clawed back, maybe just clinging on?

GOLD

The action in Gold could not be more positive, I was expecting that this rally would be driven by short selling but it is being driven by new buying and the shorts are still fighting, the war between shorts and longs is wicked. The number of open positions in gold futures has risen with the price in recent sessions, which reflects fresh buying entering the market.

If open interest instead was falling during a time of higher prices, this would suggest the rally was nothing more than short covering.

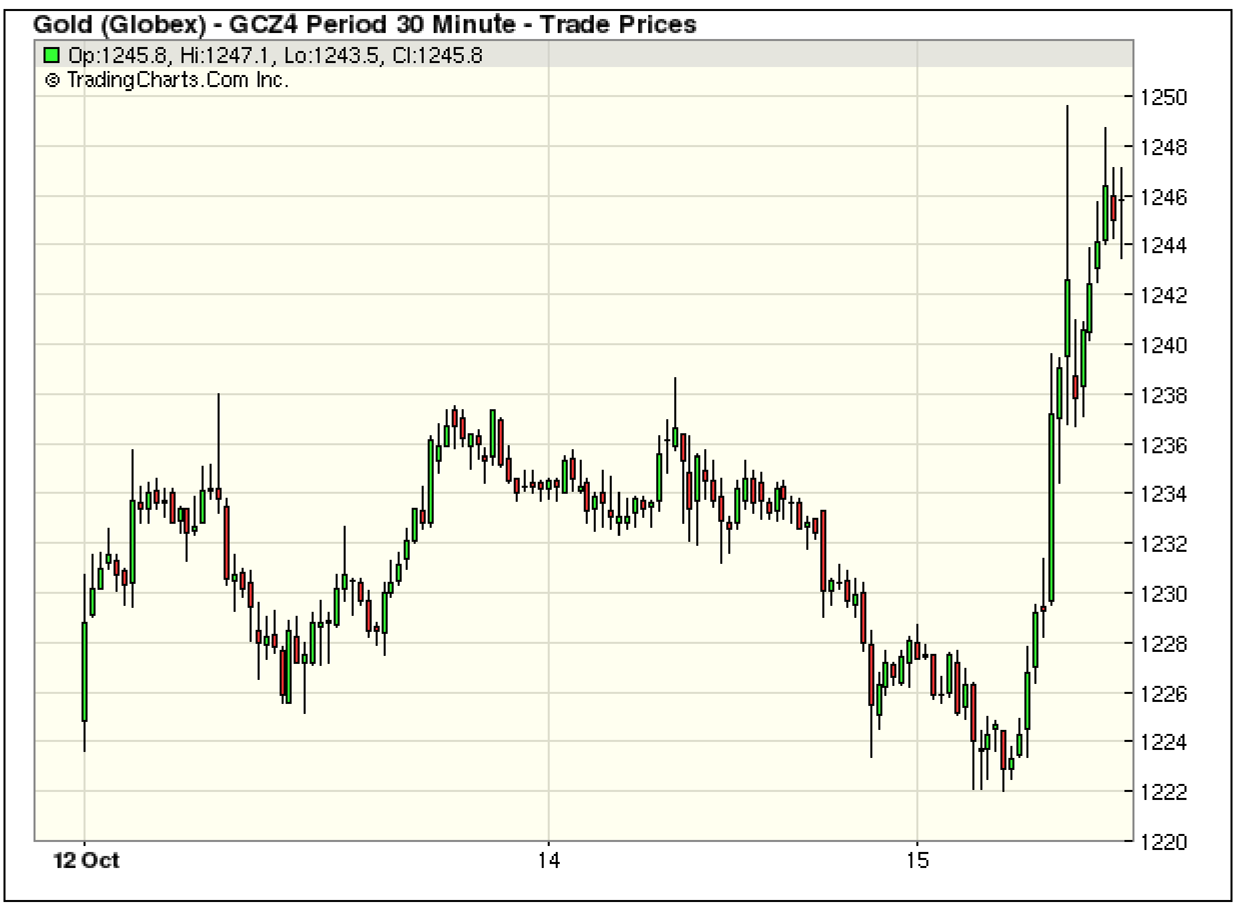
"I noticed that the bargain hunting has started," said George Gero, precious-metals strategist with RBC Capital Markets Global Futures. In particular, he pointed out that open interest in gold futures on Monday rose by 11,543 contracts. The most-active December gold contract rose $8.30 an ounce that day. Then, preliminary data for Tuesday shows it climbed another 1,360 lots. As it did so, December gold added another $4.30.

By Wednesday open interest increased several more thousand contracts.

This next intraday chart of Gold reveals the Shorts weak hand.

Notice that the price was pushed down in the late hours of the 14th and the wee hours in the morning of the 15th from around $1232 to $1222. This is the period of thinnest trading where the price can be influenced the easiest. The shorts were trying to defend their position, but when active trading began around 8 AM the shorts got trampled with Gold jumping about $25 in 2 hours.

This is very bullish because it means there is probably lots of short covering left to fuel a rally



Here is a question to ask yourself, is the market falling because of weak economic data, or are they using the weak market to get weak data out of the way? We should not have to ask that but in a day of constant intervention – it is so sad

As Richard Russel (DOW Theory fame) put it "Endless Propaganda"

http://kingworldnews.com/kingworldnews/KWN_DailyWeb/Entries/2014/10/14_Richard_Russell_-_Endless_Propaganda_%26_A_Horrifying_Endgame.html

Oil. is very interesting on perhaps the reasons for the plunge. On Sept 10th , I commented that " *I was watching the $90 level and than the $86 level. If we fall below this we could see a much larger decline and it would confirm the price is being manipulated lower."*

Yesterday Oil fell below $82 after the $86 support area gave way on Tuesday

I am showing a weekly chart so you can see the breakdown with the move well below $85, next support is in the low $70s so we are probably headed there

The International Energy Agency has sharply cut its forecast for oil demand, predicting that it will grow by 700,000 barrels per day (bpd) in 2014 vs a previous estimate of 0.9M bpd. For 2015, the agency expects demand to grow 1.1M bpd to 93.5M, (300,000 bpd less than previously thought.)

Saudi is pumping more oil at a time when there is generally weak demand, between the summer driving season (gasoline use) and winter heating season (heating oil). There is a couple theories going around why this is happening, the Saudis and Kuwait have both said they don't mind lower oil prices for a year or two and Saudi says they don't want to lose market share.

There's "no room" to achieve higher oil prices by cutting production, Kuwait Oil Minister Ali Al-Omair has told the official Kuwait News Agency. Al-Omair's remarks follow a report that Saudi Arabia is ready to accept oil prices below $90 per barrel, and even as low as $80, for up to a year or two. "S*audi Arabia doesn't want to lose market share in Asia,*" says industry expert Olivier Jakob.

This is just propaganda, there is definitly some agenda behind this peculiar move. Lower oil prices could help the economies in Europe, China and in some way the U.S. so could be part of a plan for economic stimulus?

I mentioned before lower oil prices could be used to hurt Russia – and it definitely will - so this could be another reason?

The 3rd theory is China is calling the shots. China has long term plans with Saudi and lower oil prices help the Chinese economy a lot. With the low prices and the sanctions by the West on Russia, it is like a double whammy to Russia so pressuring them to turn to China for economic/trade deals. With lower oil prices, China can drive a harder bargain as Russia is more desperate.

Whatever case lower oil is also pushing on the deflation front. It is also hurting the U.S. Economy probably more than benefiting. The higher oil price had caused a boom in fracking and significant rise in U.S. Oil production that was expected to continue. I have seen some reports that the brightest spots for economic recovery were in areas where this new oil boom was taking place and a little dot on Wall Street of course.

The stock market sell off has been steep and quick, but just a well over due correction at this point. While the change in the market is good for Gold, the mining shares have been hit in the sell off with all the other stocks. Basically the bounce back in Gold was not enough to over come this.

Not that there was a lot of selling in mining stocks, but bids or buyers went to the sidelines. On the S&P chart below, stocks are trying to cling to support around 1850. **This would be a good place for this correction to end if it is only to be a correction**

The Investment sentiment reports have improved from way over bought readings. There was a large 7.7% drop for the bulls to 37.8%, from 45.5% a week ago. September started with the bulls at 57.6% well into the risk zone. There was a jump for the bears to 17.3%, from 14.1%. The spread between the bulls and bears tumbled to 20.5%, from the previous 31.4%. It is now near normal levels for a rising market.

Ali Bubble is off quite a bit too – all the greater fools that bought the 250 million IPO shares the 1st day of trading between $95 and $100 might be thinking twice now.

The big question we need to consider is if the market goes lower, because the main drivers pushing it higher are about gone, the money printing QE has been tapered and this was the big bullish driver in the market along with hype that the economy was recovering, the FED was succeeding and interest rates would start to increase next year. **I have no doubt that this qtr. Earnings to be reported soon will be quite negative given global economics of the past few months**

If you remember the FED could not exit QE1, QE2, and their twist operation without the market tanking. So how much lower would the market have to go before the FED comes to the rescue, with more QE? Would the FED start to finally lose credibility??

There was a lot of market observers warning for some time that the FED could never taper to zero without the market tanking, perhaps they were correct.

If the market falls further, at some point the FED will conclude the market going down will weaken the economy in the same way the market going up helps the economy. Although this stimulus gets mis allocated, **when will the Fed ride to the rescue?** Will they be too late, behind the curve?

Would we have to see another 2008 before they act because they miss calculate? But the important thing to **realize is the market would then realize that the money printing spree cannot end**, credibility is loss the US$ falls and Gold soars!!!!!

At this point the Bond market would collapse too - so I will continue watching Bonds carefully. So far this time around they acted like other times and the move in bonds was stunning. They had been struggling but popped in price and this was mainly because of the flight to safety out of stocks and again the market having it all wrong, there was a lot of shorts betting that interest rates would rise (bonds fall), so these shorts had to cover at large losses.

On Wednesday the yield on 10-year U.S. Treasury notes, which moves inversely to the price, has fallen to a low of 1.868%. By contrast, it had been as high as 2.642% on Sept. 18, the day after the last meeting of the U.S. Federal Open Market Committee.

Rumors abound that there is Hedge Funds in trouble because many took large hits on 3 fronts, from the drop on their long stock positions and the shorts on their Gold and Bond positions. One or two blowups could trigger another round of volatility in the markets. **CME Group's 39.6 million contracts traded Wednesday set a record for volume, shattering the previous record by 47%, the exchange said Thursday. This highlights the large number of future contract trades un wound**

The chart on the next page is the 30 year bond. It is a weekly chart so I drew in a crude candle to represent this week when Bonds popped from the 140 area to well over 146. Shorts got trampled this week, but more important the market has totally unwound it's perception of rising interest rates and we are back to weak economy, low interest rates and probably more FED easing.

Again the markets had it all wrong most of the past year. Trades were way too crowded and everyone was on the same side, too long stocks and too short Bonds and Gold.

The next chart is the HUI Gold Bugs Index, although it broke a bit below 200, **I would consider this a triple bottom along with Gold, if it holds and actually is a quadruple bottom. This is probably never happened in the history of Gold stocks, certainly not in my history.** In fact it is extremely rare in any market, normally you here of a quadruple bottom break down, meaning it does not hold. However with the complete change in overall market out look in the past few weeks, I think the odds are high that this will hold. And it would also mean a strong long term base built over 18 months.

Now if you consider the Good, Bad and Ugly, this chart of the TSX Venture would not even make it, we need a 4th category of Horrific.

The TSX Venture gets the honor of the only market testing the 2008 lows. Do you think regulators have figured maybe there is something wrong here yet?????

Like over regulated, under funded, over taxed, fees and compliance, maybe too much shorting and computer programs. Certainly looks to me that the CSE will continue to eat the TSXV's lunch.

The nice rally that was building in 2014 was destroyed in just 3 weeks. This is the main problem effecting our junior explorers on our list.

But like any market it will find its bottom and it looks like a double bottom with 2008 is the way it will play out

A good article on the deflation
http://kingworldnews.com/kingworldnews/KWN_DailyWeb/Entries/2014/10/13_The_World_Is_Now_Rolling_Over_Into_A_Frightening_Deflation.html

******************** **UPDATES** *******************

Interesting First Majestic Silver (TSX:FR) produced 3,523,536 silver equivalent ounces during the third quarter, an increase of 5% year-on-year. First Majestic also notes that silver prices have declined 19% during the third quarter of 2014, **leading the company to hold of silver sales as they expect stronger prices in the fourth quarter. As of Sept. 30, the company has 934,000 ounces of silver held in inventory.**

Snip ....

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