THE
ADEN FORECAST
MONEY • METALS • MARKETS

MAY 2013 *our 32nd year*

COMPLEX TIMES... INVEST ACCORDINGLY

It's been a wild month.

Right after sending you last month's issue, gold fell sharply. The biggest surprise was how quickly it dropped and this reinforced that we have to be prepared for anything.

As we've often mentioned, we're in unprecedented times. That means we go with what the markets are telling us, and adjust our investments accordingly.

For now, we're staying diversified with a larger portion in stocks. We've lightened up on our metals and we feel it's justified. We also have a large cash U.S. dollar position. We think this is a good mix under the current circumstances.

TIPPING TOWARDS DEFLATION

For the past six months or so, we've talked a lot about the velocity of money and its effects. Not to bore you, but increasingly we believe it's become the most important factor in understanding the markets and the uncharted waters we're currently navigating through.

As you know, a tug of war has been going on for years between inflation and deflation. And the sharp drop in gold was yet another feather in deflation's cap.

Meanwhile, the world's central bankers have been at the helm, doing all they can to keep deflationary pressures at bay and they want to boost inflation. But despite their unprecedented global efforts, including massive money stimulus and near zero interest rates, the scales are still tipping to the deflation side. Here's why...

2008 MELTDOWN WAS START

Going back to the 2007-08 financial crisis, the world was brought to its knees. Don't forget, that was the biggest crisis and recession since the Great Depression, and for a while the global financial system was literally hovering on the verge of disaster.

The banks had lent money to everyone, and these bad loans and reckless policies resulted in the collapse of the subprime mortgage market. In an environment of extreme tension, some of the biggest lenders like Lehman Brothers went under, but others were saved to keep things from getting worse.

After that, the banks were scared, they had to regroup and get their houses in order. They obviously didn't lend money. Instead they became extremely conservative. Even worthy borrowers were not granted loans.

This played a big part in the overall economy. It didn't rebound and grow normally following the recession.

So the Fed had to pick up the slack with their super easy monetary policies to get the economy back on track. They didn't want to repeat the mistakes made during the Great Depression and, in the process, they've tripled the money in circulation since 2008.

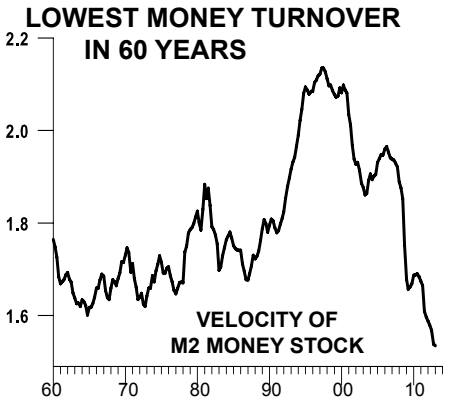
The Fed succeeded, sort of. The banks still weren't lending so the result has been a lackluster recovery and high unemployment for the past few years. Why?... This brings us back to the velocity of money (see **Chart 1**).

VELOCITY DOWN

As we've previously pointed out, the velocity has declined rapidly in recent years and it's now at a 60 year low. This is a huge deal and we're increasingly convinced this is the main factor tipping the scales toward deflation.

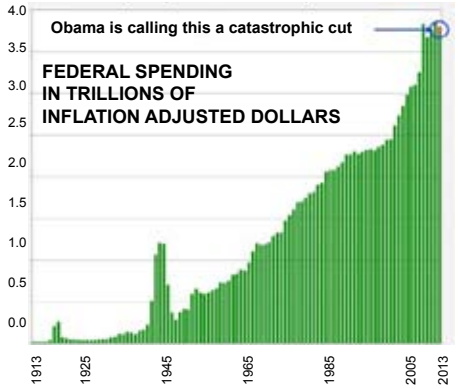
Declining velocity means the Fed

CHART 1



INSIDE

CHART 2



COURTESY: http://dailyreckoning.com

can produce all the money it wants, but this money isn't turning over. In other words, since the banks aren't lending, the money is just sitting and the Fed has no control over it.

Under normal circumstances, banks lend money to businesses for expansion and growth. Consumers borrow, and previously it was part of doing business for the banks to lend out about eight times the amount of money they had on hand.

This is called the money multiplier and the higher it is, the more it spurs robust economic growth, rising velocity and money supply. The money multiplier has also been very low since the 2008 financial crisis.

This, in turn, is a stagnant environment for inflation and that's why it hasn't surfaced like it normally would. That is, market forces have overpowered the Fed and the other central banks.

But there is some good news. According to the latest Fed Senior Loan Officer survey, banks are starting to lend, especially for businesses and commercial real estate.

This is a big deal considering they've been paralyzed for the past five years. And even though only 19% of the banks indicated they're easing up on lending, it's a start. If other banks now follow suit, then eventually we could see deflationary pressures ease up.

If so, that would certainly be the better option, but we'll see what happens. Keep in mind, the debt load is massive and the automatic spending cuts are not even causing a dent (see **Chart 2**).

Also important to consider are demographics. The world population is aging and that means they're not borrowing and buying as much as they did before.

This, together with the debt load, could keep the economy sluggish and the scales tilted toward deflation.

LOW RATES HELP... A LOT

On the other hand, we also know that interest rates are going to stay low for a couple more years. This should help boost borrowing and the velocity, as well as easing deflationary pressures.

If that happens, then we could indeed see inflation shoot up at some point in the future. The potential is clearly there and all it needs is a spark, like a shift in sentiment, to ignite inflation.

In fact, many feel that the longer deflation drags on, the longer the Fed will keep producing money and this makes sense.

We know deflation is the Fed's #1 enemy, so it's going to fight it tooth and nail. And the longer it does, the greater the future potential for surging inflation and gold.

In the meantime, all these crosscurrents make investing more difficult. As you can see on **Chart 3**, some markets have dropped sharply and one has soared, but not necessarily the way you would've expected.

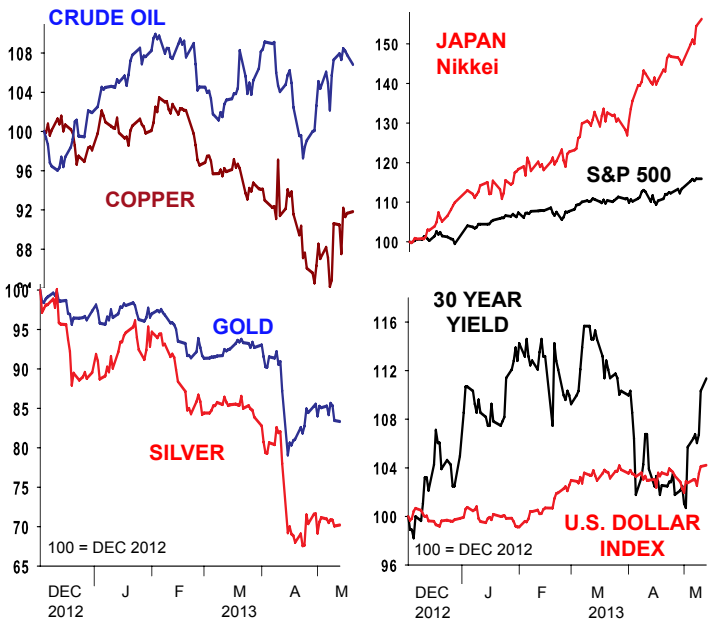
The Japanese stock market, for instance, provides a perfect example of what stubborn, long lasting deflation and extremely easy monetary policies can do.

All that money in Japan drove stocks sharply higher in the past couple of months. At the same time, the Japanese yen simply collapsed.

The U.S. is essentially on the same path, but not nearly as extreme. Will this be the eventual outcome? It could well be, but only time will tell.

CHART 3

THE UP AND DOWN MARKETS THIS YEAR



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U.S. & WORLD STOCK MARKETS

Record highs in the U.S.

The stock market is super strong, hitting new all time record highs. Its bullish momentum keeps gaining strength.

The Dow Industrials surged above 15000 and the market is likely headed much higher.

FED INDUCED BULL MARKET

We all know the Fed's easy money policies have fueled the boom in stocks. So much money has been created, it had to go somewhere and so far it's going into the stock market.

Many investors are doubtful. They're convinced the rise in stocks is just a Fed fueled bubble. But it really doesn't matter… Whether it's the Fed's bubble policies or not, the point is, stocks are bullish and you want to be in the market.

For now, stocks are the best game in town. They're much stronger than bonds, the metals, commodities and currencies. This is illustrated on **Chart 4**, which shows stocks compared to bonds as an example. But there's much more…

Low interest rates have always been bullish for stocks and we believe that's currently one of the primary factors driving stocks higher.

BEST RATE OF RETURN

Think about it… investors have nowhere to go. With interest rates near record lows and paying next to nothing, a savings account or CD simply doesn't make sense. And interestingly, rates are lower now than they were near the depths of the 2008 financial crisis (see **Chart 5**).

CHART 5

30 YEAR YIELD

As you can see, the movement in rates has been similar, then and now. But following the 2008 crisis, interest rates rebounded far more briskly. This time around they're still low and sluggish. And while that's not good for savers, it's very good for the stock market, making it more attractive.

Currently, the economy is improving but it remains sluggish. That pretty much guarantees the Fed will keep interest rates low and the money flowing.

This is a great combo, especially combined with record corporate profits and reasonable valuations. Plus, the stock market looks ahead, so its rise is also a positive sign for an improving economy.

CHART 4

STOCKS COMPARED TO BONDS

MARKET STRENGTH ATTRACTING INVESTORS

As you'd expect, mainstream investors are increasingly moving into the market. The new record highs are attracting attention, leaving the fears following the steep market drop of 2008 in the rear view mirror (see **Chart 6**).

By hitting new highs, the U.S. stock market has now recouped those losses and, again, that boosts the stock market's appeal. But we can't stress enough the importance of low interest rates.

CHART 6

U.S. MARKET... THE STRONGEST

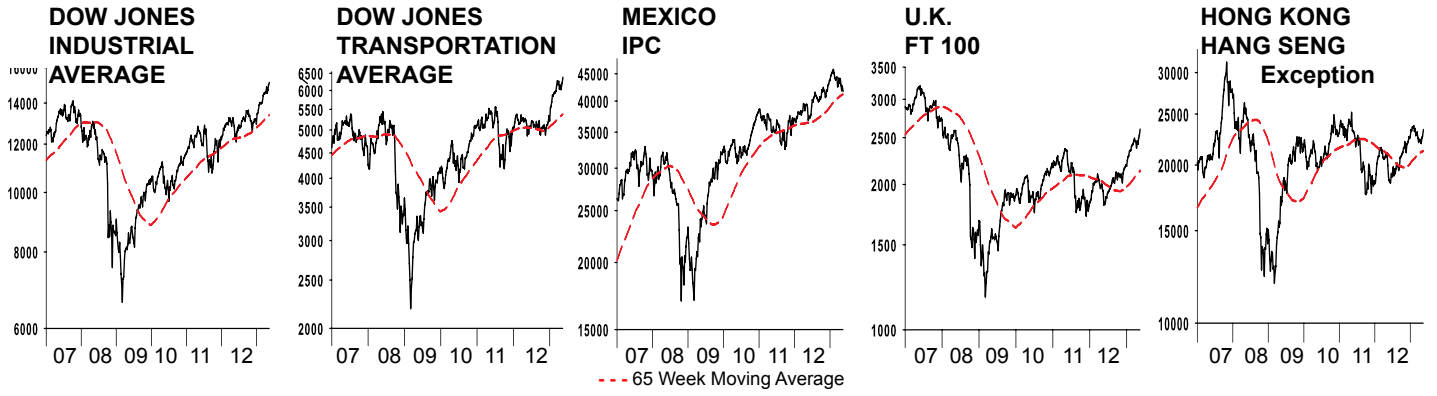
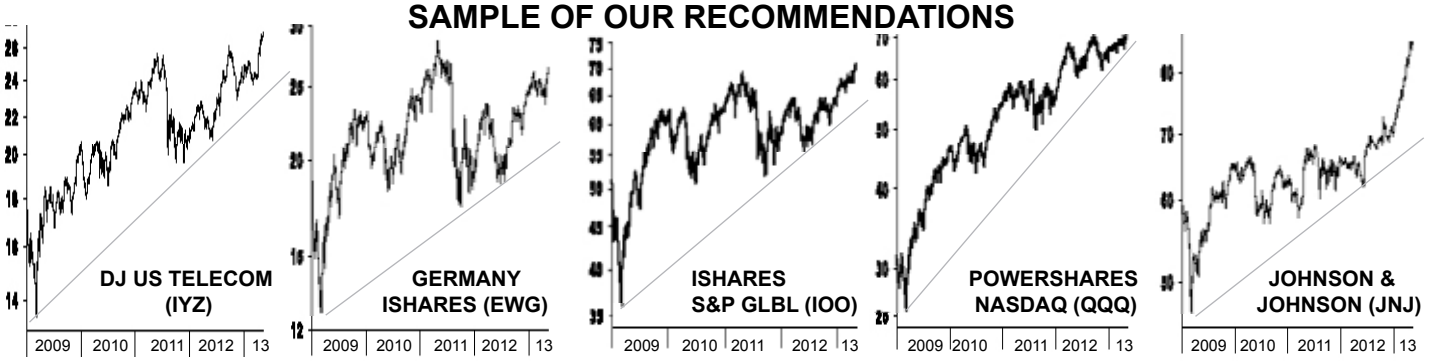


CHART 7

SAMPLE OF OUR RECOMMENDATIONS



Baby boomers heading into retirement age are not getting any income from their savings or cash retirement accounts. That means they have to increase their risk factor somewhat by going more heavily into stocks to make up for near zero interest rates.

BLUE CHIP RISE & MORE

For starters, investors have primarily been buying into the bigger, high quality dividend paying stocks. These are the blue chip stocks that're considered the safest for long-term growth and income via consistent dividends.

These are stocks like Johnson & Johnson, Coca Cola and Wal-Mart, which we've been recommending and they've been good performers (see **Chart 7** as an example). But now investors are kicking it up a notch.

Tech stocks are picking up steam and so are some of the global stock markets. Here too, low interest rates and strong earnings are fueling the rises.

You may recall that these markets had been lagging somewhat, but that's no longer the case (see QQQ and IOO on **Chart 7**). Instead, they're regaining their strength and that's yet another bullish sign.

It means investors are comfortable enough to invest in stocks that're generally considered more risky than the staid blue chips. So, they should all continue to do well.

Tech stocks, for example, are still very cheap. And the same is true of many of the world stock markets.

Plus, don't forget, there's still a mountain of cash sitting on the sidelines and most money managers are bullish. This alone could drive stocks to sharply higher levels.

DON'T FIGHT THE FED

There's an old saying in the stock market and it's so true... "Don't fight the Fed." Well, we're not. We're staying with the Fed and we hope you are too.

The bottom line is this... As long as the Fed keeps buying bonds, providing easy money, and keeps interest rates at super low levels, stocks are going to rise further.

As you know, there is never a sure thing in the market. But this is about as certain as it gets, so stay with it.

And since stocks have been rotating and taking turns being the strongest, that's also why we're keeping our stock recommendations diversified (see **Chart 8**). We have some blue chips, tech stocks, global stocks, energy, a utility and a couple of resources, and we think that's a good mix.

WHAT TO DO

Several of you have asked if it's too late to buy, assuming you didn't buy at all last year, or if you have a very small position in stocks...

We believe stocks are headed higher. For new buyers it would be ideal to buy on a downward correction, especially if the "sell in May and go away" syndrome comes to pass. But the ideal moment may not come. So we'd go ahead and buy at least some now, and then buy more when stocks do correct. In other words, average in.

Currently, we'd buy new positions in Powershares Nasdaq (QQQ), Johnson & Johnson (JNJ), Dow Diamonds (DIA), S&P Global 100 (IOO) and DJ Telecom (IYZ) as well as our two new recommendations DJ Trans iShares (IYT) and Consumer Discret SPDR (XLY).

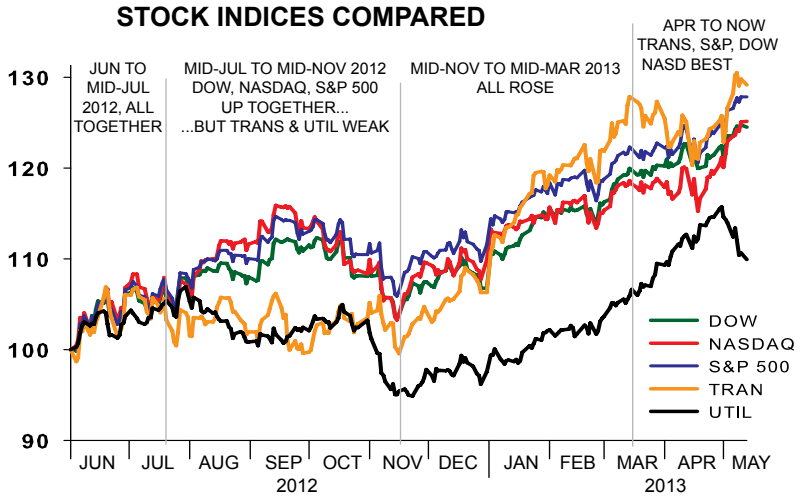
You've also asked if it's too late to buy Japan. It has soared, mostly due to Japan's super easy money policies and the collapsing yen.

In this case, we'd be more cautious, stay on the sidelines and let it go.

For now, stocks will remain super bullish with the Dow Industrials, Nasdaq and S&P500 above 14500, 3250 and 1550.

CHART 8

STOCK INDICES COMPARED



U.S. INTEREST RATES AND BONDS

Low rates to stay... for how long?

Interest rates have been volatile lately, but they shot up this month. This is not unusual considering what's going on within the big picture.

UNUSUAL TIMES UNUSUALLY LOW RATES

As you know, U.S. interest rates have literally plunged over the past 32 years. Back then, they were about 15% but they're currently almost at zero, and near the lowest levels in over 200 years! Now, that's unusual.

This has led to lots of speculation that the huge bond bubble is ready to burst, especially once inflation picks up. Many also feel that interest rates can't keep declining because they're already too low and they've been falling for too long. The next direction, therefore, has to be up.

As you know, we felt the same way, but we're beginning to question this. So this month let's take a contrarian view...

FOLLOWING JAPAN

The U.S. has been following the Japanese experience via stimulus and low interest rates. This has been ongoing in attempts to kick-start its economy. But it hasn't worked in Japan where GDP has remained near 0% for several years.

More impressive, low interest rates haven't done the trick either. As you can see on **Chart 9**, with a couple of exceptions, Japanese interest rates have been below 1% for 18 years. And they're super low in other countries as well (see **Chart 10**).

In the U.S., rates have been below 1% for the past four years. But if the U.S. keeps following Japan's lead, then interest rates could stay low for years to come.

We know 32 years is already a long time for interest rates to be on the decline. But looking back at interest rate history, it's not that abnormal. Twice, for instance, U.S. interest rates declined for 26 years, and in the late 1800s there was a 58 year drop, which ended up being the longest one.

We're not saying history is going to repeat. But if it does, then interest rates could decline or stay low for another 25 years and it still wouldn't match the longest U.S. interest rate drop. And while this may seem outrageous, this scenario is not out of the question.

CHART 9

U.S. & JAPAN 3 MO RATES: 20 YEAR VIEW

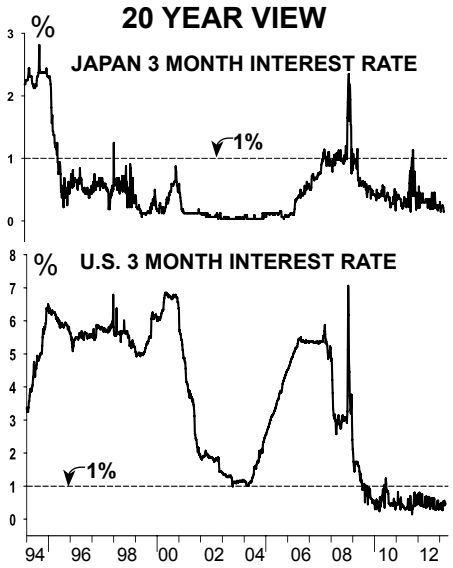


CHART 10

THREE MONTH INTEREST RATES

JAPAN	0.25
EURO	0.25
U.S.	0.40
BRITAIN	0.65
CANADA	1.23
AUSTRALIA	3.12

SLUGGISH WORLD ECONOMY

The U.S. economy is sluggish, and so is the rest of the world. But focusing on the U.S., which is generally one of the stronger developed economies, history again provides a real eye opener.

Note that economic growth since 2000 has only averaged 1.8% (see **Chart 11**). And going all the way back to 1790, the only decade that was worse was during the Great Depression.

So looking at growth and interest rates, it's very clear the U.S. (and the developed world) is truly in uncharted waters. That's not just a catch phrase, it's real. That is why anything is possible.

The Fed has been buying $85 billion in bonds each and every month to stimulate the economy. And it's going to keep doing this until unemployment falls further and/or inflation rises. This too will keep downward pressure on interest rates for the time being.

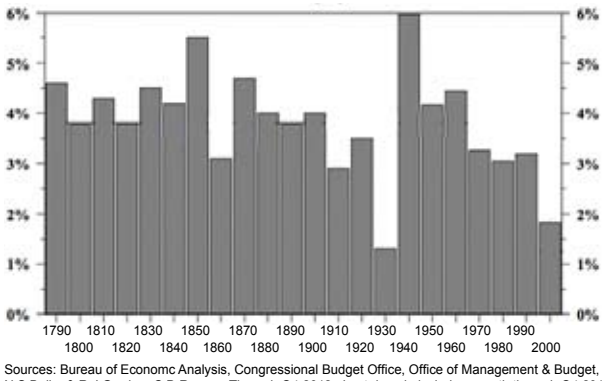
The same is true of the sluggish economy. As long as it struggles, bond prices will remain firm and interest rates will stay low, and volatility will likely continue (see **Chart 12**).

BUT... STAY FLEXIBLE

Looking at the flip side, however,

CHART 11

REAL GDP 1790-2012
DECADE AVERAGE GROWTH



Sources: Bureau of Economc Analysis, Congressional Budget Office, Office of Management & Budget, N.S.Balke & R.J.Gordon, C.D.Romer. Through Q4 2012. Last decade includes growth through Q4 2012

COURTESY: Hoisington Quarterly Review / Mauldin Economics

CHART 12

there are still many factors pointing to higher interest rates and lower bond prices in the months ahead.

Take a look at the technicals, specifically the head and shoulders top that is forming on the bond price (see LS, H, RS on **Chart 13**). This formation would be confirmed if the upchannel is broken and bond prices could then fall to near their 2008 and 2011 lows.

In other words, the 30 year yield would trigger this confirmation if it were to rise and stay above 3.25%. If so, it could then likely move up to near the 4% level.

Also keep in mind, the U.S. dollar is another key factor. Since bonds are denominated in U.S. dollars, the outlook for bonds depends a lot on what happens to the dollar.

DOLLAR & YIELDS: Move together

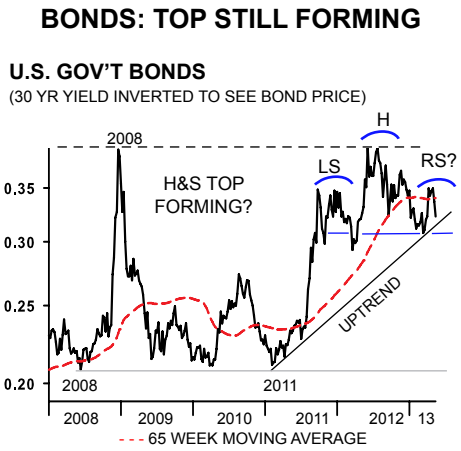
As you'll see next, the U.S. dollar has been holding up ST, but it's still vulnerable LT. And once the dollar resumes its long-term downtrend, it'll make bonds far less attractive, especially to international investors. That is, interest rates would have to rise to make U.S. bonds more appealing.

As we showed you last month, the inflation-deflation barometer is still favoring gold over bonds, despite gold's recent fall.

As long as that's the case, it suggests that it's just a matter of time until inflation rears its head in reaction to all the money that's been produced.

If not, then deflation will have the upper hand.

CHART 13



All factors considered, the interest rate signals are not yet firmly conclusive, but we'll keep watching as we wade through this uncharted territory.

In the meantime, it's still okay to keep bonds if you have them, even though we're not officially recommending them. If you sold your bonds, that's fine too.

For now, interest rates are likely headed higher as long as the 30 year yield stays above 2.95%.

CURRENCIES

U.S. dollar: ST strong... LT questionable

The U.S. dollar is the world's reserve currency. This is a privilege that is unique on the international stage.

This privilege is usually bestowed on the world's most powerful country. That country usually has the strongest military and the most fiscally sound economy.

RESERVE CURRENCY STATUS: A privilege

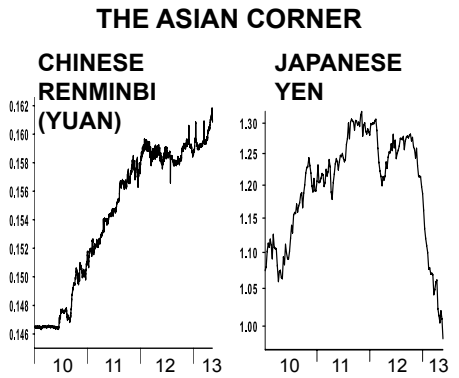
Over the centuries several countries have held the world's reserve currency title and, interestingly, this usually changes every 100 years or so.

From 1450 to 1530, for example, Portugal held the top spot (80 years). From 1530 to 1640, Spain was the top dog (110 years). After Spain, Holland followed for 80 years, from 1640 to 1720. The next 95 years belonged to France (1720 to 1815).

In more recent times, relatively speaking, the British empire ruled the seas and many countries from 1815 to 1920. As you'd expect, the British pound was the world's reserve currency for those 105 years.

Then the U.S. took the top position, which it's maintained for the past 93 years. And based on this historical time rotation, its dominance is likely in the final stretch...

CHART 14



BUT WHY THE CHANGES?

Sooner or later, the reserve currencies have generally followed the same pattern. In one way or another, the superpower devalued its currency until it was no longer desired by the international community.

This was usually due to excessive spending to finance wars and other expenses, huge debts that

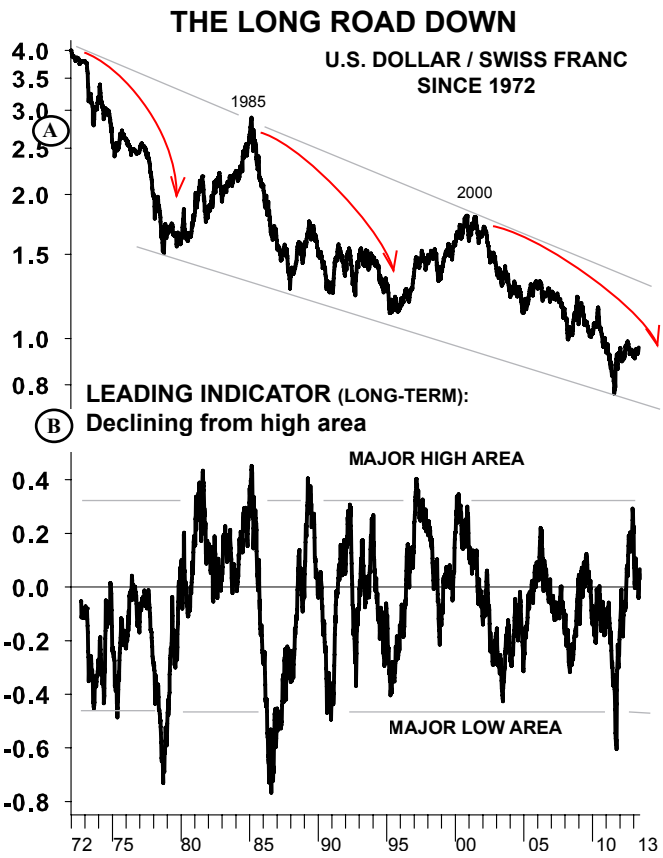
couldn't be repaid, and the currency lost its value. It then stopped being the reserve currency and it was replaced by another more desirable country and currency.

This is really nothing new. It's happened hundreds of times throughout history. It happened in ancient Rome and it's happening today.

Normally, when a currency holds the world's reserve status, most other countries will keep their excess funds (reserves) in that currency, which is currently the U.S. dollar.

In recent years, however, there's been a change and it's gaining momentum. As the U.S. dollar has declined over the years, it's reflecting the old excessive spending and too much debt pattern (see **Chart 15A**). It's slowly been devalued and, like the former superpowers, the rest of the world is taking action.

CHART 15



CHANGING CURRENCY RESERVES

Many countries have been decreasing the U.S. dollar part of their reserves, and their euros too. Instead, they've been diversifying into other currencies and gold. The Australian and Canadian dollars have become more popular choices.

Plus, as we've often pointed out, many countries are simply skipping over the U.S. dollar. In other words, they're trading in their own currencies, thereby eliminating the U.S. dollar from their transactions.

China in particular has made trade agreements with dozens of countries using their own currency, the renminbi (see **Chart 14**). Their latest deal was with France and rumors continue to swirl that China will probably be the next reserve country, eventually taking that role from the U.S.

This is obviously not going to happen overnight, but China has indeed been laying the foundation. And so has the U.S.

As you know, the U.S. has been spending like mad, the debt load is unsustainable, the economy is sluggish and it's printing tons of money to pay for all its expenses. The QE program continues full speed ahead to boost the economy.

And even if Bernanke retires later this year, Janet Yellen will probably take his place. She's a big fan of QE, so it'll likely continue, meaning the U.S. dollar is nearly guaranteed to fall further in the months and years ahead.

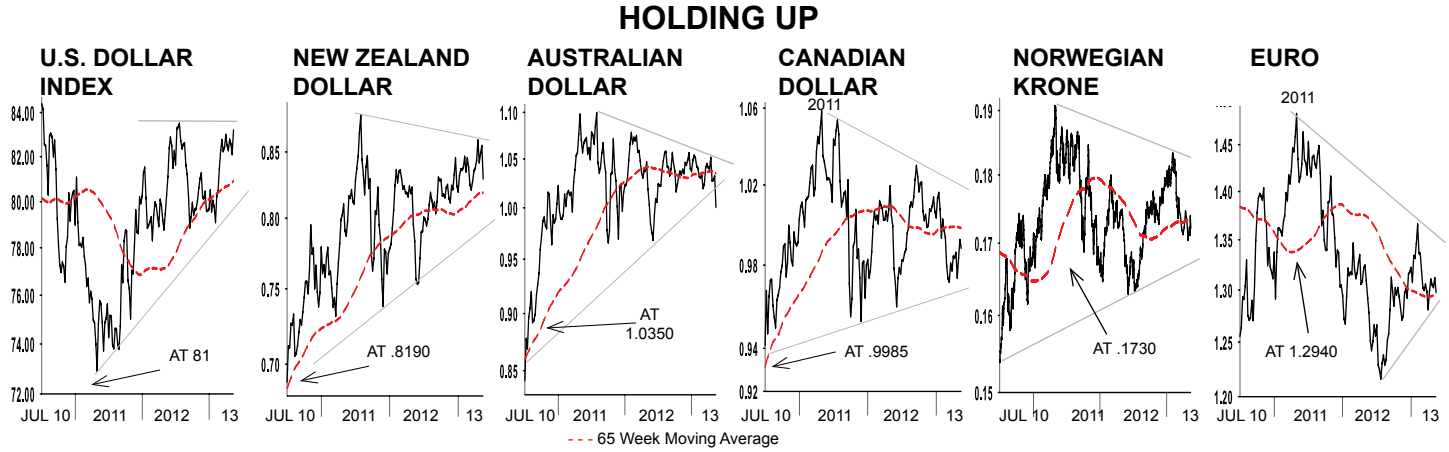
STRONG U.S. DOLLAR ST

Like we said, these major shifts are slow moving, but we're quite sure the dollar is well into the final stretch.

For now, however, the U.S. dollar index is showing renewed strength. It's at a nine month high and it's likely headed higher, especially if it stays above 83. In fact, it won't show real weakness until the index declines and stays below 80 (see **Chart 16**).

Once that happens, the euro will move sharply higher since it's the dollar's offset currency (again

CHART 16



see **Chart 16**). But that's not the case for now and we advise selling. The ongoing problems in the Eurozone are taking their toll on the euro and so is the stronger U.S. dollar. It's also putting downward pressure on most of the currencies.

Meanwhile, the yen is plunging. Its drop is in reaction to Japan's own QE type stimulus, which is relatively three times larger than the U.S.'s (again, see **Chart 14**).

China's slowing economy has taken a toll on the Australian dollar, as well as the decline in their interest rate. It has turned bearish and we recommend selling it (see **Chart 16**).

The Canadian dollar and Norwegian krone are primarily oil currencies and they're also weak. But the New Zealand dollar has been one of the strongest currencies.

Currently, we recommend selling the currencies we've been holding. The New Zealand dollar is the only exception. Most funds, however, should be kept in U.S. dollars since it's now the strongest.

METALS, NATURAL RESOURCES & ENERGY

A wounded bull

It's already been a month since gold fell almost $200 in two trading days. This head-spinning drop damaged the bull market. It broke the back of a STRONG market, but that doesn't necessarily mean the mega uptrend is over.

Our first potential downside target level for gold at the $1300 to $1450 level was reached. And while gold has since been backing and filling, we could see gold decline further in the months ahead before a bottom is found.

DOWN, BUT NOT OUT...

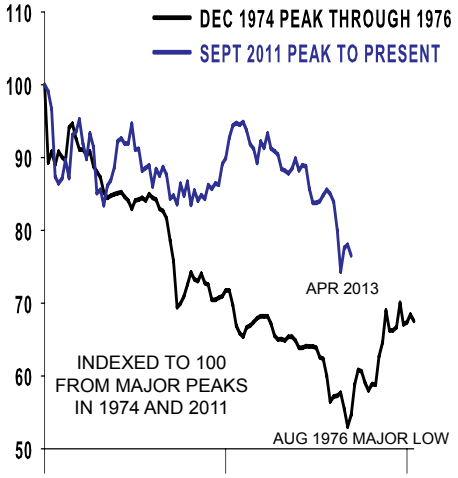
As of the mid-April low, gold is down about 19% for the year. If gold ends the year near these low levels, it'll be the first time in 12 years gold has had a down year. Assuming this happens, the 660% rise from 2001 to 2011 would be down about 28% from the peak, which isn't bad in perspective.

During the last 12 years, gold rose without inflation, with a war on terror, during the worst financial crisis in decades, through an unprecedented debt build up and during years of economic sluggishness.

This time period also saw the U.S. dollar decline amid growing doubts of its reserve currency status. And it's been a time when many countries have protected themselves from uncertainty by buying the most gold in 50 years. That's because our present economic situation is nearly unparalleled in U.S. history.

CHART 17

GOLD: COMPARING DECLINES



... WILL RECOVER

This almost $200 gold fall is coming on the heels of a sluggish gold price since Sept 2011. Gold tested the $1536 level twice in the last 1½ years, but this time around took the cake.

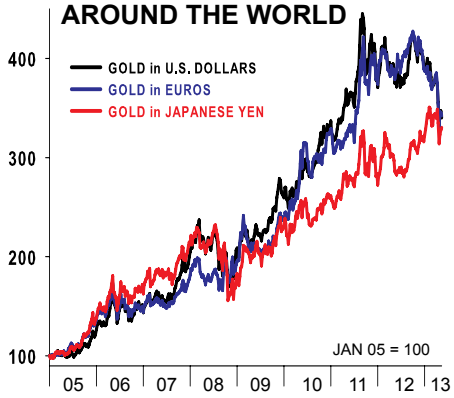
Gold's two day fall was the worst since 1980. And as investors lost confidence in gold, April also ended with the world's largest ETF, GLD, having its biggest monthly outflow since it began.

In hindsight, it makes sense that with so many sell orders near the lows, it triggered a snowball decline.

In fact, investors were already turning against gold. But many feel the large banks manipulated gold by calling an end to the bull market. Citigroup, Goldman Sachs, Credit Suisse and Societe Generale all joined in the chorus.

CHART 18

GOLD PRICE AROUND THE WORLD



For now, this drop has sparked a lot of controversy between the gold lover's camp and the gold haters. It's a passionate situation. And depending on your outlook, you could say both are right.

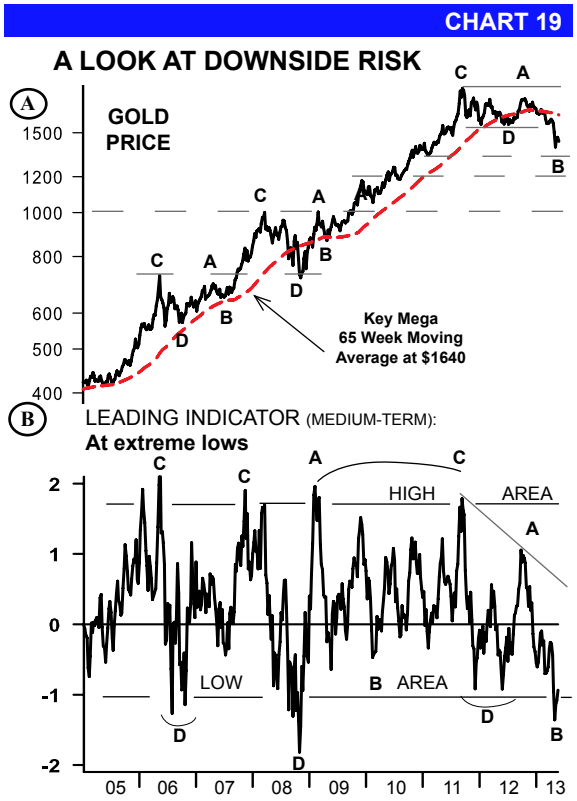
We are of the camp that the bull is wounded but it will recover. It may take time to recoup and we'll likely see more volatility before any kind of decent rise develops.

THE 1974 -1976 EXAMPLE

This bearishness can only be compared to 1976 when gold reached a low in-between two bull markets. It was amazing.

Gold fell 50% from its almost $200 high in December 1974 to its $102 low, and it took almost two years to do this. That was enough to call it the, "Great Gold Bust"... in spite of its 460% run up from 1970 to 1974.

Often, the length of time a decline takes tends to be more bearish than the decline itself. In 2008,



for instance, gold fell almost 30% in eight months. It was fast and furious but sentiment didn't have a chance to turn too bearish. Plus, almost everything else was worse.

Today is similar to 1976 because of the time it's been taking. Investors were getting turned off by the sideways gold market for the past 1½ years before it plunged last month. And especially so because the stock market has been soaring this year.

Chart 17 shows you today's gold fall from its September 2011 record peak compared to the 1974-76 time period. We indexed the peaks to 100 so you can see true time and percentage decline comparisons.

Interesting here is, so far, gold has given up almost 30% from its peak and it's getting closer in time to the 1976 lows.

That is, gold fell 50% in 1976. If today's decline is similar, we could see gold near $1,000 by June. That would be the same type of fall in time and price as in 1976, and it's the worst case scenario.

GOLD: Still bullish in several currencies

Gold's bull market really took off in 2005 and it coincided with the launching of GLD, the then new gold ETF, in late 2004. This made it easy for investors to buy gold and it surged.

Gold broke above $500 and it rose strongly in all currencies (see **Chart 18**). Gold moved in lockstep until 2010, then it changed.

Gold broke above $1,000, the 2008 peak level, and it again took off like a bandit. But gold rose much further in dollar and euro terms, than in yen terms.

Currently, however, this chart shows **a bullish picture for gold regardless of the currency**. It's saying the gold price got away from itself and it's now at the same high level in terms of all currencies.

This could be why the Group of Seven is tolerating a crashing yen and an unprecedented liquidity program to get Japan's economy going.

But it's still to be seen how much longer until it becomes a problem. We could see a currency war downstream, which would of course be very bullish for gold.

GOLD UNDER PRESSURE

Gold continues to feel pressure when worries surface that the Fed will cut back on its easy monetary policy, yet it's very unlikely, at least for this year.

Currently, the stronger U.S. dollar of late is the real pressure on gold.

As long as the dollar is strong, we'll continue to see gold struggle. The collapsing yen, for example, is bearish for gold because it pushes up the dollar.

The dollar has been boosted by better economic news, like the improving labor market and stronger retail sales. And while this could go on for a while longer, it's unlikely to be a sustained dollar rise.

Meanwhile, let's take a look at the downside and what to keep an eye on...

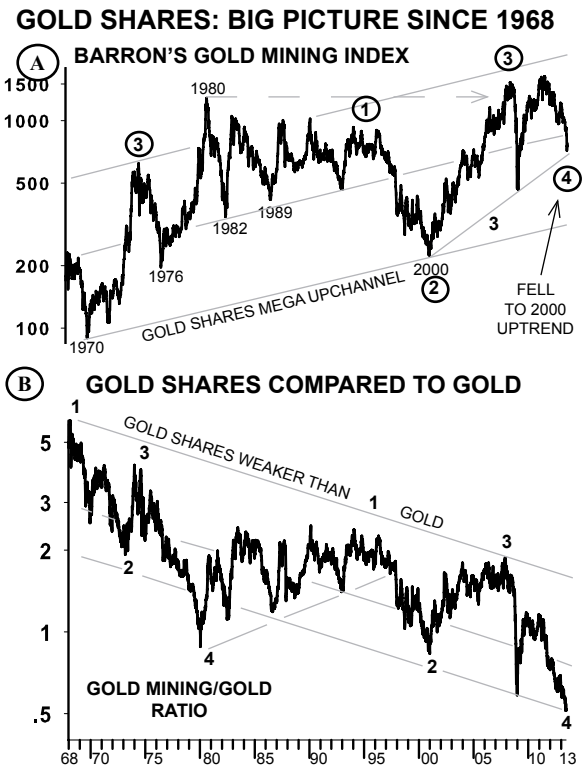
Chart 19A shows the stepping down levels. Now that $1536 has been clearly broken, it's become the first key resistance level.

The next support is the 2011 lows near $1320 (which also happens to be the intraday low for the latest fall). This level is important because if it's broken, we could see gold slip below $1200, near the 2010 low. And in a worst case, the 2008 peak near $1000 is the ultimate support.

Our indicators show that this $1000 level would be an extreme case and if tested, it's unlikely it would stay there for long.

Notice that our favorite indicator has fallen to an extreme low area (see **Chart 19B**). Most interesting

CHART 21



is that it only went below -1 in two other extremes, in 2006 and in 2008, and in both cases it preceded strong upmoves in gold.

In fact, considering the wide double D low in 2011-2012, the indicator never fell below -1. It now finally has, which is saying the downside is far more limited than it was before.

Let's keep an eye on $1320 and $1536 this month. The $1320 to $1536 levels identify the wide band. Within the band, if $1360 is broken gold could decline to $1320.

On the upside, if gold rises above $1450 it could bounce up to $1536. And in a better situation, we could see the 65-week moving average tested at $1640.

HISTORY REPEAT?

The bigger picture, however, shows more downside is possible.

Chart 20A shows the gold price since 1968. Here you can see the two great bull markets in the 1970s and since 2001 on a semi log scale. This also shows that gold could technically decline to its bull market uptrend since 2001 near $1000 but it would still be in a strong and firm bull market.

Note that gold's second half of the bull market, from 1976 to 1980, gained much more than the first half. Will history repeat this time around? We'll see.

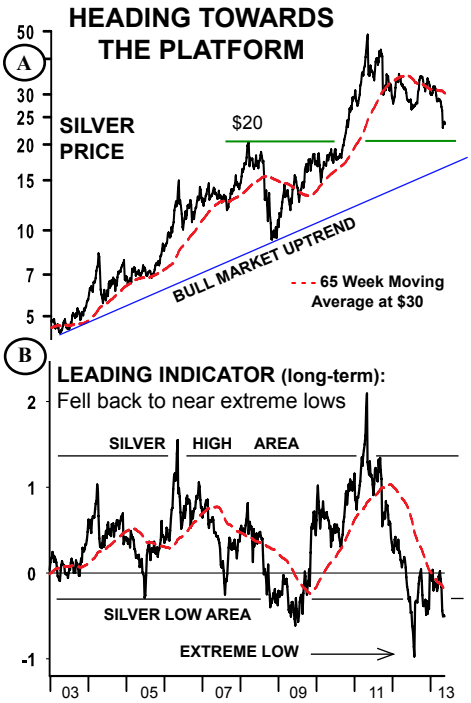
Important in this big picture is the leading indicator. It never made it to the blow off high area during its 12 year run. And it's now at the 2001 lows. If gold tests its major uptrend, we'll likely see the indicator fall into the extreme low area, or at least the low area.

If this happens, we'll be buying with both hands!

WHAT TO DO

In our update of April 16, we advised lowering your metal's position to 15% (from 30%; we first lowered it to 30% last February). We also recommended primarily keeping

CHART 22



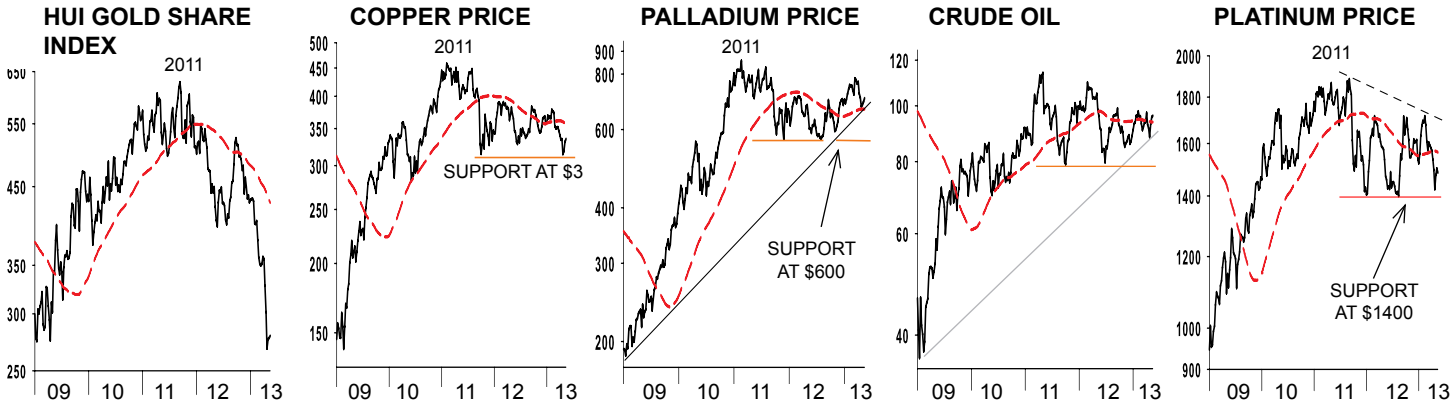
your physical gold and silver core positions. That is, the coins and bullion you plan to keep over the long-term, riding through periods of weakness.

All factors considered, we felt it was best to lighten up, primarily in the shares and ETFs. But if your 15% position includes physical and paper assets, that's okay too.

The main point was to lower your metal's position, which we feel is justified, and keep the proceeds in U.S. dollar for the time being. Once the lows look like they're near, we'll be raising our position again.

For now, many of you are concerned with GLD and ETFs in general. Paper gold holders were certainly

CHART 23



quicker to sell, mainly because it's easy. Plus, the intrinsic value isn't appreciated like it is with physical gold holders.

But it's unlikely to see physical gold and paper gold go their separate ways. The ETFs, however, are fairly new, not even 10 years old, so they have yet to be tried and tested.

Many of you also asked how gold would perform in a deflationary environment. We are in one right now and, frankly, much will depend on the soundness of paper currencies.

Since we are in uncharted waters, we'll continue to go with the flow and stay with the trends. It's really the best way.

Our friend and coin dealer, Dana Samuelson, told us about the craziness they had in their office during the gold drop. While it's now calming down, the premiums, especially on silver surged to the highest since the 2008 aftermath.

Be it the U.S. Mint, the Canadian Mint or Johnson Mattley, they can't keep an inventory of silver coins. It's been madness and scramble.

Many are buying, demand is high, and central banks are taking advantage of weakness and buying too. The love-hate passion for gold is in full swing.

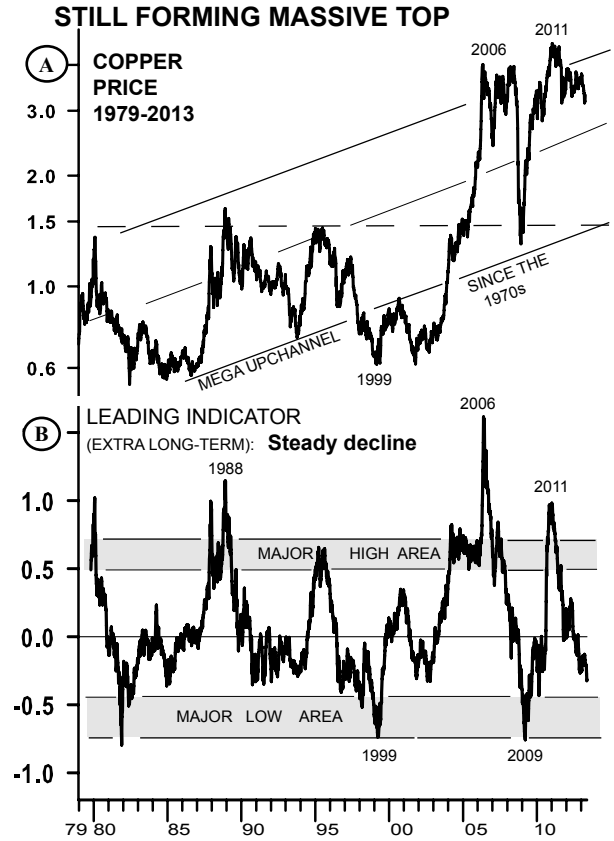
GOLD SHARES: Bombed out

Gold shares continue to reach even better, cheaper prices. There's little doubt it's the market investors are loving to hate, especially with the stock market rising. The gloom is pretty thick, but we think a small position in gold shares is still okay.

Chart 21A shows a big picture of gold shares since 1968. Notice how gold shares essentially resisted near their 1980 peak, and they've fallen to their 2000 uptrend.

This is happening at a time when the gold shares to gold ratio has dropped to an extreme record low (see **21B**). As you can see, the ratio has favored gold all along, but it also shows that gold shares are clearly bombed out compared to gold.

CHART 24



Note the 1 - 4 movements in the late 1960s -1970s and a similar 1 - 4 movement since the 1990s. Except for the number 3 move, gold has always been stronger than gold shares during bull markets. Also, gold shares are better than gold during bear markets.

BOTTOM LINE: Gold shares are poised to pop up versus gold and in dollar terms. In the 1980s, for example, gold shares soared after the gold peak in 1980, reaching their peak 8-9 months later.

SILVER: More like gold in 1976

Silver no sooner completed its two year mark since the peak, and it fell even further. It's given back over 50% from its April 2011 high. Yet considering it rose more than 1000% from its 2002 lows to this April peak, this decline hasn't been bad at all.

It just shows how volatile silver can be. Silver has the characteristic of either moving quietly, like it's been doing since the decline, or moving wildly. There's not much in-between.

Chart 22A shows silver since 2003. Here you can see if silver falls to the $20 level, it wouldn't hurt the main 11 year uptrend.

And if it does, you can see the indicator would clearly move into an extreme low area. This indirectly says silver is unlikely to fall lower than this.

If silver now stays below $22.80, then $20 is likely. On the upside, silver would look better above $26 and $30.

RESOURCES: Key to real global economy

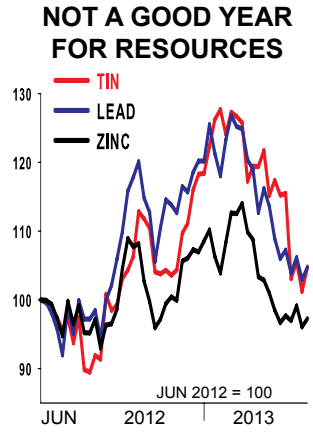
The resource sector has been weak this year. The sluggish economies in China, the Eurozone and the U.S. have kept demand down.

The base metals are under-pressure, and copper is starting to dip below $3. This is a key level for copper because it's been the support area since reaching its peak in 2011 (see **Chart 23**).

Looking at copper's bigger picture since 1979 on **Chart 24A**, you can see a massive topping process that's been going on since 2006.

This is telling us that if $3 is clearly broken, we could see $2.50 reached as the leading indicator declines further. This would be a bad sign for the global economy.

CHART 25



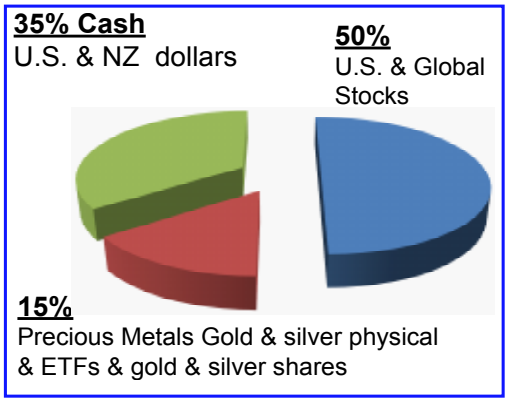
Copper's major support is at the $1.50 level, but it seems unlikely it'll reach that extreme. Copper will remain under pressure until it closes back above $3.45.

Crude oil and palladium look similar. Oil has been firm this month and it looks good above $93.50.

Palladium bounced up from its 65-week moving average and it's firm above it at $665.

OVERALL PORTFOLIO RECOMMENDATION

The markets were wild again this month. Gold fell sharply and quickly but stocks surged, hitting new record highs. Interest rates moved higher and so did the U.S. dollar. This all means we go with what the markets are telling us, and adjust our investments accordingly. We're staying diversified, but we're increasing our portion in stocks and we've lightened up on our metals' position. We also now recommend keeping a large U.S. dollar cash position and we feel this is a good mix for now.



PRECIOUS METALS, ENERGY, RESOURCE RECOMMENDATION

Gold and the other metals fell sharply last month. Since then, they've been backing and filling but they could decline further before a bottom is found. In our update of April 16 we advised lowering your metals position to 15% (from 30%). We also recommended primarily keeping your physical gold and silver (coins and bullion) core positions and lightening up, mainly in the shares and ETFs. But if your 15% position includes physical and paper assets, that's okay too. The point is, lower your metals exposure, which we feel is justified for the time being. Once the lows look like they're near, we'll again increase our holdings. Currently, the bull is wounded but it will recover. In the meantime, gold and silver have strong support at $1320 and $20, respectively.

U.S. AND GLOBAL STOCK MARKET RECOMMENDATION

The stock market is the best game in town. It's hitting new all time record highs. Low interest rates have been very bullish for stocks and the market has the Fed on its side. We believe stocks are headed to much higher levels. Most of our recommended stocks are doing well and we're increasing our stock position to 50%. Keep the stocks and ETFs listed on the right. For new buyers, buy some now and buy more when stocks correct. Currently, we'd buy new positions in Nasdaq (QQQ), Johnson & Johnson (JNJ), Dow Diamonds (DIA), S&P Global 100 (IOO) and DJ Telecom (IYZ), as well as our two new recommendations DJ Trans iShares (IYT) and Consumer Discret SPDR (XLY). For now, sell Xstrata (XSRAF) and ISE Glbl Copper (CU).

CURRENCIES RECOMMENDATION

The U.S. dollar index is showing renewed strength. It's at a nine month high and it's likely headed higher, especially if it stays above 83. The dollar index will not turn bearish until it closes below 80. We recommend selling the euro, Norwegian Krone, and the Canadian and Australian dollars. Keep most of your proceeds in U.S. dollars. The New Zealand dollar is also okay to hold.

INTEREST RATE & BOND RECOMMENDATION

Interest rates have been volatile lately but they shot up this month as bond prices tumbled. Bonds are forming a top and if the 30 year yield rises and stays above 3.25%, bond prices could fall to their 2008 and 2011 lows. The yield could then move up to near the 4% level. Like we've been saying, interest rates are likely going to stay low for quite a while, so even though we're not recomending bonds, it's still okay to keep them if you rely on bonds for income. If you sold bonds, that's fine too. Rates are likely headed higher and bond prices lower if the 30 year yield stays above 2.95%.

Note: Shares, funds & ETFs are listed in the box in order of strength per each section. Keep the ones you have on the list.

OUR OPEN POSITIONS

GOLD & SILVER ETFs AND SHARES

Palladium	PALL-NYSE	
Central Gold Trust	GTU-AMEX	
SPDR Gold Shares	GLD-NYSE	HKE:2840
iShares Comex Gold	IAU-NYSE	
New Gold	NGD-AMEX	TSX:NGD
Silver Wheaton	SLW-NYSE	TSX:SLW
iShares Silver Trust	SLV-NYSE	
Central Fd of Can	CEF-AMEX	TSX:CEF-A

STOCKS AND ETFs

PowerShares Nasdaq	QQQ-Nasdaq
Cons Discret SPDR *	XLY-NYSEArca
DJ Trans iShares *	IYT-NYSEArca
iShares S&P Glbl 100	IOO-NYSEArca
Dow Diamonds	DIA-NYSE
Microsoft	MSFT-Nasdaq
Johnson & Johnson	JNJ-NYSE
DJ US Telecom	IYZ-NYSEArca
Germany iShares	EWG-NYSEArca
DJ US Fn SVC iShrs	IYG-NYSEArca
Energy Select SPDR	XLE-NYSEArca
Coca Cola	KO-NYSE
Hong Kong iShares	EWH-NYSEArca
Wal-Mart	WMT-NYSE
Agribusiness Mkt Vec	MOO-NYSEArca
Templeton Emerging	EMF-NYSE
Procter & Gamble	PG-NYSE
American Elec Power	AEP-NYSE
Mexico iShares	EWW-NYSEArca
Vietnam ETF	VNM-NYSEArca
US Global Res	PSPFX-NYSE

CURRENCY ETFs

Canadian dollar	FXC-NYSEArca
Euro	FXE-NYSEArca

* New positions