

The Futures/Intermarket Report August 24, 2007

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The Futures / Intermarket Report Trading the World's Markets

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A bottom for silver? Silver has been correcting since late July and fell over \$1 in on the August 16 session and has since been trading in a small sideways channel. The August 16th fall looks like a classic panic sell off and may have created a bottom from which silver will climb higher. There are a number of technical indicators supporting the idea of a bottom in silver. Firstly, let's see what the smart money is doing. Analyzing commercial traders is a tool we've used in the past for this column and it has helped signal some important moves in various futures markets. Figure 1 shows the current position of commercial traders in relation to the past 3 years. The commercial index which is represented by the dark green line shows that commercial traders have one of the largest silver positions in the past 3 years which is likely to lead to a rise in the metal. The same chart also shows the typical seasonal patten for silver in the bottom panel. August has traditionally been a bottom as highlighted by the blue vertical line son the chart, and this increases the odds for a bottom as well. If you look closely, commercial traders have had large position increases in silver in the past 3 years near the August time period, that pattern is repeating itself this year as well and it seems that the smart money is expecting the typical seasonal pattern to repeat itself this year.

Figure 1 Chart by genesisft.com Another supportive factor for a price increase in silver is the fact that most advisors (dumb money) is bearish on silver. Only 37% of advisors are bullish and last week it was less than 25%, a level that typically coincided with other bottoms in the metal as you can clearly see with the blue vertical lines in figure 2.

Figure 2 Chart by genesisft.com Another way to help determine when a rise in silver is about to occur is to see when silver begins to outperform gold. An easy way to do that is to analyze silver prices divided by gold prices. I took that analysis one step further by detrending the ratio. Detrending the data allows for the technical analyst to easily see any cyclical tendencies in a security. It appears that silver follows an approximate 40 day cycle that is highlighted by equidistant blue line in figure 3. As you can see, silver has bottom approximately every 40 days for the past 2 years, and it is currently in the time frame for a bottom.

Figure 3 Chart by genesisft.com After studying smart money and advisor sentiment, seasonality, and cycles, we can see that there is the possibility for a bottom in silver. Signs of a trend reversal in price will confirm all of the analysis made today and most likely lead to a move approaching at least \$13.

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