$22/oz - silver's Rubicon

By Ben Turney — Thursday 30 May 2013

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In recent pieces I've shown how both copper and gold have reached crucial levels of support on their MIDAS charts. Now it's the turn of silver.

The silver market has been pretty uninspiring for a quite a while now. In the aftermath of retreating from its summer 2011 highs, the price was range bound for the next 18 months. Suddenly, on the 12th of April, it went into freefall along with everything else metal related.

Trailing copper and gold, it took silver until May 20th to reach its own Rubicon. But as with those other two metals the crucial question now is will it cross?

To put this into context, above is the 10 year MIDAS chart for silver.

There are two levels of support to note; JUN2003 (the pink line) and NOV2008 (the blue line)
Until April's stampede for the exit, NOV2008 support had been the primary support for the 4½ year silver bull market. It was confirmed twice during 2009 and in the last year and a half provided two superb trading opportunities; in December 2011 and between June and July last year (both circled in red). For a few days, last month, it looked like a third opportunity was shaping up but the sudden break below this important level of support was troubling. The collapse strongly suggested that the latest bull market was well and truly over.

However this needn't be as bad as it sounds.

As shown in the diagram above, silver's 10 year old JUN2003 support is $22.

The older a confirmed support line is the higher its significance. Silver's JUN2003 support was last breached for three months in late 2008. This proved to be the beginning of an incredible run higher.

If silver is now able to consolidate around its current level over the next few months, this could be a decennial buying opportunity.

But.

Before we get too excited, there are some warning signs to be aware of that could indicate near term difficulties.

First there is still a notable divergence between gold and silver. The current gold:silver ratio is 61.9. Since 1985 the average gold:silver ratio has been about 45.7. This suggests that gold and silver are mispriced. One is too cheap relative to the other or the other is too expensive

There was a lot of speculation at the end of last year and the start of this that the high gold: silver ratio was bullish for the prospects of silver. Of course what this commentary failed to take into account was the possibility that gold was overpriced. This is still the case.

The second warning concerns gold's MIDAS chart. As I showed in my recent article gold's next major level of support is $1,197/oz, although it is still trying hard to complete a bullish double bottom pattern at the current support ($1,397/oz). If gold fails in this endeavour then further falls are to be expected and $1,197/oz would seem a reasonable target. Another sell-off in gold will almost certainly hit sentiment for all the precious metals and could drag them all below their current lows, silver included.

Finally the outlook has changed a great deal in the last five years. Although silver differs from gold in that it has many industrial applications, much of the last bull market was driven by inflation expectations. Logically the scale of money printing should have led to runaway inflation. So far this has failed to materialise. Though it is too early to say with any confidence that this is not still a danger, there is an increasing consensus that deflation is more of a threat. In the medium term this could still be positive for silver, but in the interim this might hold the price back.

Overall silver at $22/oz looks like it is a speculative buy. The long term significance of JUN2003 support should not be underestimated. The wider market is still skittish, so the risks should be clear, but the longer silver manages at least to consolidate in this area the greater the chance of a sizeable rally. Bear in mind though, if a new bull market starts in 2013 it will likely be driven by very different factors than the last.
Ben Turney is a smaller company's investigative writer with an interest in metals prices