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Why silver might be a good buy at \$20 an ounce

By Myra P. Saefong, MarketWatch

SAN FRANCISCO (MarketWatch) — Silver didn't quite turn out to be a bargain at around \$30 an ounce early this year. At \$20, however, it could be a steal, if you're careful.

"Most indications are that silver is at or very near a bottom," said Paul Mladjenovic, author of *Precious Metals Investing for Dummies*. The massive selling of silver futures contracts during the first half of this year "is very over-done and created some extraordinary bullish conditions."

Silver futures (CNS:SIU3) closed Thursday at \$20.15 an ounce, down almost 34% year to date. About a month ago on June 27, prices settled at \$18.53, their lowest since late August 2010, according to FactSet data, tracking the most-active contracts.

Silver's declines have well outpaced that of gold's (CNS:GCQ3) steep drop of 21% year to date. Copper's (CNS:HGU3) down roughly 13%, platinum's (NMN:PLV3) lost almost 7% and palladium (NMN:PAU3) has gained 5% this year.

"Silver is a more emotional market than gold, meaning it often has extreme upside and downside moves [more] than other metals," said Alan Knuckman, chief market strategist at Trading Advantage, a market education and trading training firm. Silver prices were cut nearly in half from the highs around \$35 in September to the recent low near \$18.

"The rewards are sometimes greater in silver when you are [on] the right side," said Knuckman.

Mladjenovic, meanwhile, referred to silver's current prices as "artificially low" and said they'll "push marginally productive silver mines to close and this will shrink supply" as demand for the metal continues to grow.

Is the gold bounce for real?

Brendan Conway explains why gold ETFs are rising even as individual investors are selling. Plus: Hidden dangers of ETFs and ETNs.

Even after the metal's huge losses, however, not all analysts are quick to call a bottom for the white metal.

And they have good reason: Forecasts for an end to the silver selloff [back in February](#) turned out to be wrong, and prices instead leveled off before falling even more.

Blame that on silver's usually high volatility and its [split personality](#) as an industrial and precious metal.

Bullied silver

Indeed, the silver market has been jostled around by demand indications from economic data around the world and pressured by moves in gold, which in itself has been shoved around by changing perceptions over the U.S. Federal Reserve's monetary stimulus.

Fed Chairman Ben Bernanke [said last week](#) that "nobody really understands gold prices." And given that silver is so closely tied to the moves in gold, maybe that means no one really understands silver.

SIU3 21.38, +0.97, +4.77%

GCQ3 1,335.80, +22.90, +1.74%

September silver vs. August gold



But remember, Bernanke was only [partly right about gold](#). It's not that people don't understand the yellow metal, it's that it's tough to understand — and traders and investors can look at silver's key influences for a better view too.

Of course, that includes gold.

"For the last several years, silver has moved with gold, rising a little higher on the rise and falling lower on the fall, including during the last three traumatic months for precious metals," said Julian Phillips, a South Africa-based contributor to SilverForecaster.com and GoldForecaster.com.

Gold prices finished the [second quarter with a loss](#) of over 23%, while silver dropped nearly 32%.

"Nothing has shaken this relationship" between gold and silver, said Phillips. "So the driving force behind a solid rally in silver will have to be one in the gold market."

Among the headwinds for both precious metals this year were Europe and a strengthening U.S. dollar, said Paul Herber, portfolio manager of the Forward Commodity Long/Short Strategy Fund

“Gold and silver built up a huge following due to fears surrounding a Greek exit of the euro and in a worst-case [scenario], the complete unraveling of the euro,” he said. “The fear has now subsided from the market and we have seen a commensurate pullback in precious metals.”

At the same time, however, silver and gold have to contend with a [strengthening dollar](#) as changes in the value of the greenback affect prices for the metals.

The dollar index (NYE:DX) , which tracks the greenback’s movements against six other major currencies, has climbed about 2.5% so far this year.

Silver demand and its price also “fell as the market’s view changed to a perception that financial assets, such as stocks and bonds, have become less risky,” said Thomas Winmill, portfolio manager of the Midas Fund (MFD:MDSX) . Year to date, the Dow Jones Industrial Average (DJ:DJIA) has climbed almost 19%.

“With apparent fixes put in place in Europe’s banking systems, in the U.S. government’s fiscal situation and China soft landing, among others, the likelihood of the debasement of fiscal liabilities ... seems to be less,” Winmill said.

Economics 101

So why might silver prices climb from here?

After the metal’s hefty price drop, the basic rules of supply and demand are set to come into play if they haven’t already.



Reuters

Silver prices have suffered a bigger drop than gold’s this year.

“The basic influence on silver is the supply/demand relationship and there are potential issues for lower supply and higher demand at these lower price levels,” said Michael Haynes, chief executive officer at online precious-metals dealer APMEC Inc.

The low prices “can adversely affect the secondary or scrap source of supply,” which account for 29% of total supplies, he said, and can substantially increase jewelry demand, which account for 31% of demand.

Interestingly enough, the iShares Silver Trust (NAR:SLV) , which SilverForecaster.com’s Phillips, refers to as the main U.S. vehicle for silver long-term investors, has seen “strong accumulations while there were falls in the SPDR Gold Trust,” Phillips said.

[Read more on how the iShares Silver Trust has recently traded near \\$20.](#)

Silver holdings in SLV have [climbed to](#) about 10,428 metric tons, after falling well below 10,000 metric tons about a month ago.

In contrast, [gold holdings](#) in the SPDR Gold Trust (NAR:GLD) , which had played a large part in the yellow metal’s price drop this year, stand at about 927 metric tons, down from just under 970 metric tons a month ago.

“The fundamentals for silver are remarkable in that in an economic recovery, silver demand will rise ... and when the economy is pulling back, the fear factor makes silver an attractive investment,” Phillips.

Still, a little bit of a wait won’t hurt.

Even at around \$20, Adam Koos, president of Libertas Wealth Management Group, said silver “might be a good buy,” but he’d rather wait to see more consolidation and support before feeling comfortable buying in.

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SilverForecaster.com