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SILVER - base pattern, or bear Flag??...

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The principal conundrum facing us at this time, and thousands of other traders and investors is to figure out whether the bottom is in, or whether we continue on down from here. In last weekend's [Gold](#) and [Silver](#) Market updates, we came down on the side of the bottom being in for reasons that we are going to review again today, and in the [Financial Armageddon](#) article we looked at the worst case scenario where the bottom is not in, at least for PM stocks, which would be what would could result if Europe falls apart in coming months.

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You will recall that we have opined in the past that Europe's state of extreme crisis could be eased, at least temporarily, if they would only stop bickering and get on and print money, in the style of the US, and kick the can down the road in time honored style. If they do in fact do this, and the US continues to as well, then the current deflationary scare would ease, and markets could recover and of course gold and silver could resume the upward path. In respect to this the following comments by a subscriber, Jeff, are of interest...

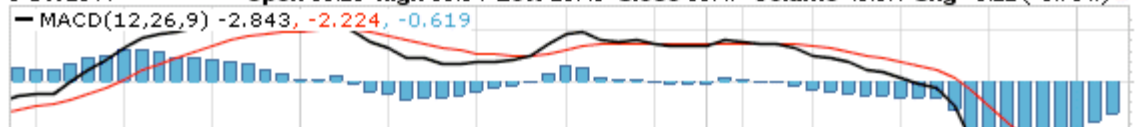
"Remember the game's fundamentals. Bankster-leftists are in charge. (Goldman-Sachs were Obama's number one donors. Big Government and Big Banking, working together.) THEY WANT TO PRINT MONEY. They allow these market crash / "deflation" scares to happen periodically (if indeed they don't engineer them), as a way to gain political cover for printing more money. Right now, the market is rising on new-ish Bernanke promises to "do more to help the economy". I don't know if this is a reversal or just noise, but it highlights my point. Do NOT expect a full, 2008-or-worse style of crash. It will

only happen if the bankster-leftists think it's needed to overcome political (Tea Party) resistance to more QE. They hope it won't be necessary - they hope to be able to announce (or at least implement) more QE very soon. That's why you see the bullish COT on PMs, and bearish on the dollar."

If Jeff is right and they don't feel the need to go the whole distance with a full-on 2008 style deflationary scare to squash resistance to QE, and Europe avoids meltdown and papers over the cracks with its own QE program, then we are looking at a bottom for the Precious Metals sector right here and now, and as you know there are technical indications that the sector has indeed bottomed.

Let's now review the charts again in the light of these observations and what we discussed in the Financial Armageddon article.

\$SILVER (Silver - Spot Price (EOD)) CME © StockCharts.com
5-Oct-2011 **Open** 30.25 **High** 30.64 **Low** 28.43 **Close** 30.47 **Volume** 43.9K **Chg** +0.22 (+0.73%) ▲



SILVER: 3-month Chart

Silver is now massively oversold on its MACD and neutralizing histogram (blue bars) is increasing the chances of a rally.

Ⓢ \$SILVER (Daily) 30.47
MA(50) 38.70
MA(200) 36.08



COULD THE CURRENT TIGHT PATTERN BE A BEAR FLAG, to be followed another severe drop? - it could, but the appearance of a highly bullish "Dragonfly Doji" and the strongly bullish COTs make it more likely that silver has hit bottom and that a base is now forming.

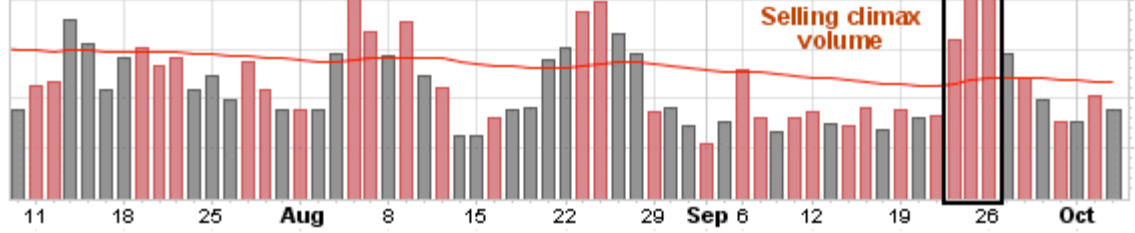
Many silver longs are understandably traumatised after the brutal selloff and normally at this point we will see a base area develop that allows time for sentiment to recover. However, COTs are now so bullish - & bearish for the dollar, that a recovery could commence a lot sooner than we would otherwise expect, and possibly almost immediately. We are now in the "accumulation zone" and any dips towards the low of the bullish Dragonfly doji" should be bought aggressively and any such dips would be viewed as providing a great opportunity to load up with Call options.

An enormous bullish "Dragonfly Doji" ends the rout. →

RES.

ACCUM. ZONE

Volume 43,945, EMA(60) 58.16K

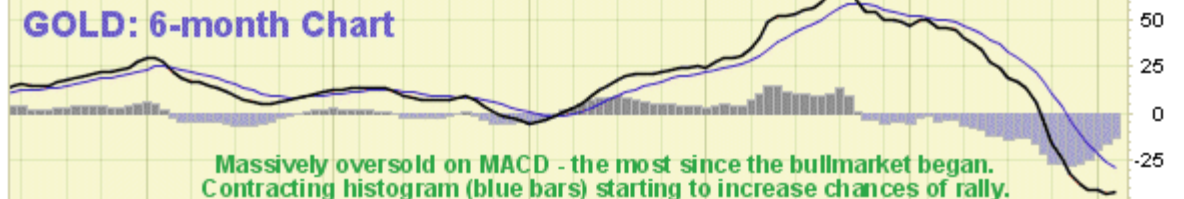


\$GOLD (Gold - Spot Price (EOD)) CME © StockCharts.com

5-Oct-2011 **Open** 1626.80 **High** 1648.90 **Low** 1596.80 **Close** 1644.40 **Volume** 146.9K **Chg** +18.40 (+1.13%) ▲

MACD(12,26,9) -42.229, -29.067, -13.162

GOLD: 6-month Chart



\$GOLD (Daily) 1644.40

MA(50) 1751.21

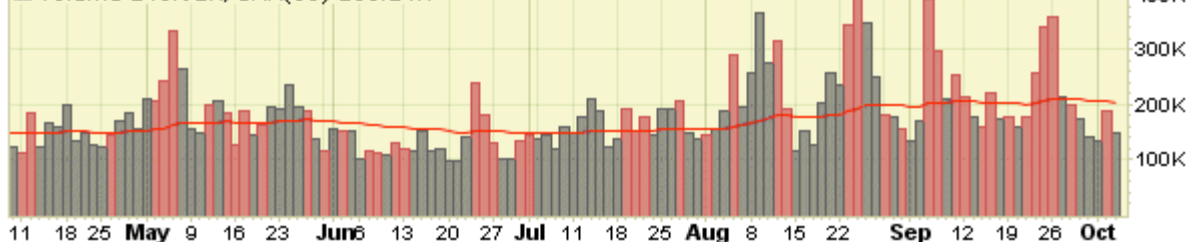
MA(200) 1532.50

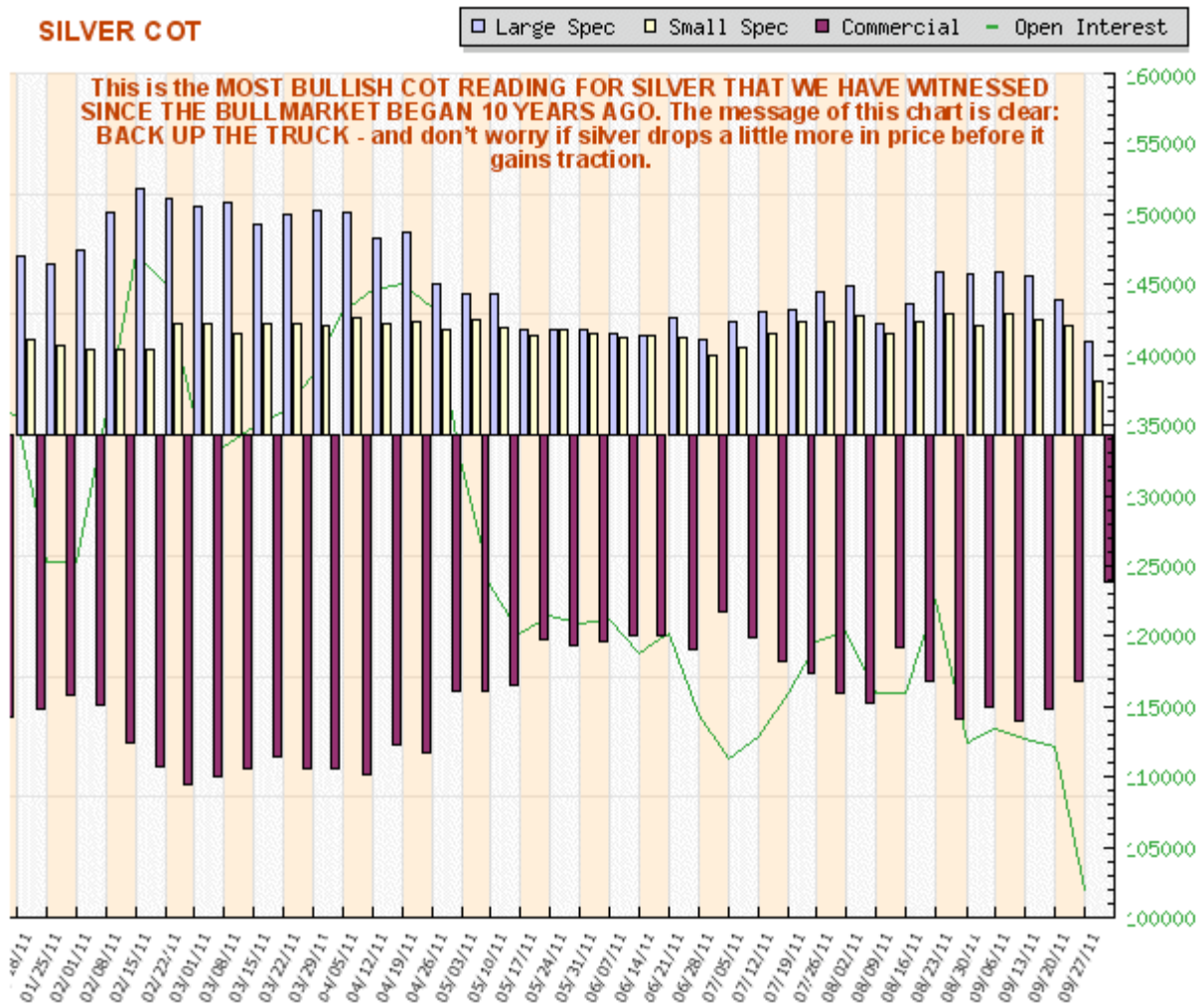
Gold is now AT ITS MOST OVERSOLD SINCE THE START OF THE BULLMARKET 10 YEARS AGO. Normally, after such a vicious plunge, we would expect to see further downside. However, several key indicators suggest that it will bottom here and turn higher again. One of these is the latest COT which is at its most bullish for a long, long time, and a big one is the US dollar COT - the Commercials have been piling on the shorts in the US dollar and now have an unusually big position, suggesting that a dollar reversal is imminent. It could be that Europe's problems are going to "solved" by increased unity and the generous application of QE - which would be very bullish for gold.

Looks like a classic reaction by gold back to support above the 200-day moving average.



Volume 146.92K, EMA(60) 203.24K





On the silver chart we can see that the plunge in silver was extraordinarily severe, and raises the possibility that the current holding pattern might be a bear Flag, which would be bad news indeed for anyone long, as if it is a Flag then another severe downleg can be expected to occur within weeks. However, there are two important factors which indicate that it is not a Flag, and that silver bottomed just above \$26 on Monday of last week. One is that a giant "Dragonfly Doji" candlestick showed up on that day which is normally strongly bullish and calls for reversal. The Dragonfly Doji is a variant of the "bull hammer" where the open and close are at the same point at the high of the session, and it is even more bullish than a hammer. The other indication is the last COT chart that we looked at at the weekend, which is extraordinarily bullish, even taking into account the raising of margin requirements which has resulted in some distortion. In addition gold's drop halted at the traditional place for a correction to end - at support above its 200-day moving average. For all these reasons there is considered to be a much better than even chance that silver is bottoming here. A big reason for the severity of the plunge in silver is

believed to be that small speculators, egged on by cheerleaders, had racked up a very high level of leveraged positions, and Big Money, having access to this data, simply put the squeeze on them to drive them out of their positions at knockdown prices as they were forced to disgorge by margin calls.

If a bottom is forming in silver here, then it makes sense for us to start looking at silver stocks to buy, which is what we are going to do. We have time, as the damage to sentiment occasioned by the plunge means that it will probably be 2 or 3 weeks before any significant rally can gain traction. This should give us time to make our selections, but also time to see if the pattern in silver develops in a satisfactory manner.

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