

SELLING JUNIORS? – YOU MUST BE KIDDING!

by
Eric Hommelberg



It sure has been a quite a week for gold and HUI.. Both seemed to be plunging in a deep black hole and again many inquiries came my way asking whether or not it's time to sell since so many analysts turned bearish lately.

I urge to re-read my previous piece 'Gold It's a Bull Market Stupid' since this piece an update on that one. But let me start off first by answering a burning question (for many):

Q: Should we sell our gold shares these days?

A: No, why should we sell our core asset which continues to rise month by month even during corrections like these.. Believe it or not but our core asset (Discovery TOP 10) doubled in value since gold reached its peak of \$730 early May this year. Even on a blood red day like last Thursday when the HUI dropped by 15 pts two of our Discovery TOP 10 stocks performed very well, Buffalo jumped by 9% while Aurelian gained 3.5%.. The very next day (while HUI was more or less unchanged) Aurelian jumped again by 7% and Buffalo by 5%..

END.

Well, guess that doesn't need any further explanation here, the bottom line is:

Companies in discovery stage will do well anyhow no matter what the gold price does in short term!

Readers following us closely do own our Discovery TOP 10 and are protected well against any (short term) down-trend in gold.

Now why are juniors making discoveries so profitable? It goes far beyond the scope of this update to explain in detail but the key-point is that major producers are forced to acquire juniors because of the need for more reserves, here's why:

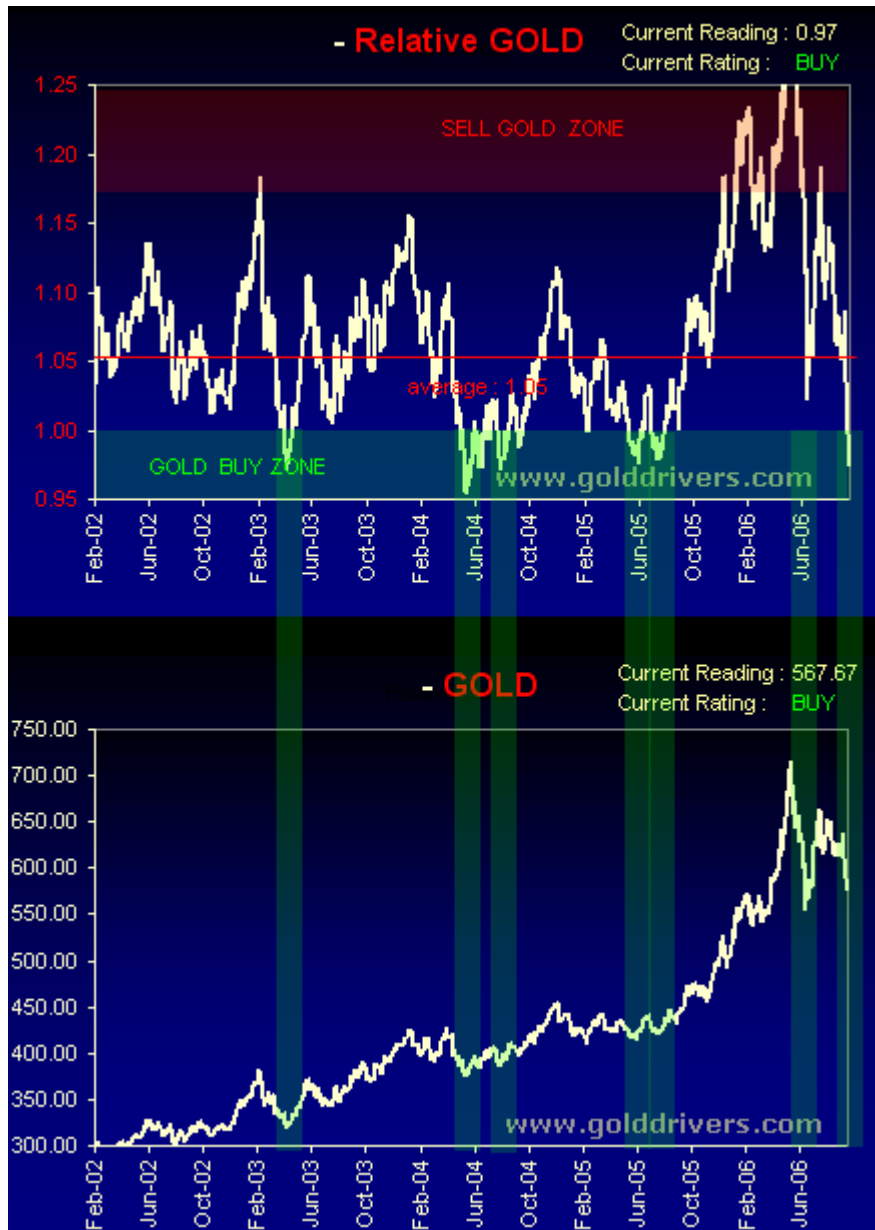
- The industry is not replacing the reserves it is mining every year
- High grade mines are running out of ore.
- If Gold were \$1000 / oz , it still takes four to seven years to open a mine.
- The industry isn't going to be able to respond immediately to higher gold prices.
- Reserves will be depleted in 10 years at current annual production rates
- The industry needs some major new finds desperately. Since 1999 only a very few world class gold deposits have been found.
- Majors are forced to acquire juniors because of the need for more reserves

OK, enough about holding onto your discovery stocks, let's follow up on gold's recent decline and whether or not we're approaching a major bottom anytime soon..

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As discussed in my previous piece ‘Gold- It’s a Bull market Stupid’ I explained how the rGold chart nailed every major bottom of the last 4 years. Now let’s take a peek first at the update rGold chart and see what it says right now:



As you can see rGold dropped further in the green ‘BUY’ zone this week which translates itself into a better risk/reward ratio from an investment point of view. In other words, buying gold at these levels could be a prudent thing to do..

Now should we buy gold now?

The answer is ‘NO’ since gold still finds itself in a downtrend and we simply have to wait patiently till it breaks the recent downtrend to the upside..

Q: What is the maximum downside potential from here on?

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A: Well, if history could be of any guide then we see that previous correction ended in the 0.95 – 1.00 rGold area. A rGold value of 0.95 translates itself into a gold price of \$560 these days..

Sure enough this is not a prediction that gold will drop to \$560, it's just a worst case scenario according to the rChart..

Now let's take a peek at the gold chart itself and draw a bottom line which reflects rGold'st worst case scenario and an interesting pattern emerges:



The two charts do suggest the following:

- Gold is reaching severe overbought conditions thereby making a short term rebound more likely than not..
- The latest down-turn (C-line) is the latest (killer) move down of a correction which started early may this year.
- If current down-trend continues (C-line) it will bounce on solid \$ 550 - \$560 support within a week..

If current down-trend (C-line) will be broken to the up-side within a week we can expect a short term upward bounce for gold due to the severe oversold conditions we're witnessing these days...

The entire correction in gold which started early May will be over when the D – line will be broken to the upside which could take another couple of weeks to unfold.

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Will it happen?

My bet is yes since the physical demand is picking up steam quite rapidly now. The Indians aren't going to delay their weddings due to high gold prices, in fact they are profiting from the recent dip in gold and started buying more aggressively. Gold trades in Mumbai reached about 800 kilos a day from 250 kilos, a week earlier..So there's good physical demand under \$600 which will make it difficult for the short players to push gold down much further from here..

The fact that physical demand is picking up steam indeed is recognized by GFMS as well.

GFMS (usually to be found in the bearish camp) projects a gold price of \$700 before year end and over \$800 next year..

GFMS CEO Paul Walker said during an interview on Mineweb:

Well the end of this year we I think we'll see \$700 gold, or certainly very close to \$700 gold before the end of this year. I think it's going to be a bit of a roller-coaster in the next three or four months in this market. As we go into 2007 – again, to make a call on when the US economy is really going to turn. Now I've indicated in the past that I think the US economy is showing the strain. Sooner or later this is going to break, and if it does break in the near term then \$800 is very much on the cards next year. END.

Summary:

- **Gold is reaching severe oversold territories and may rebound anytime soon**
- **Physical demand picking up steam this season which makes it hard for the short players to push gold much further from her on.**
- **Owning discovery stocks is the most profitable investment strategy since companies making discoveries will perform good anyhow no matter what the gold price does in short term.**

Eric Hommelberg is the Editor of The Gold Discovery Letter and The Gold Drivers Report.

www.golddrivers.com,

is one of the best informed websites on gold.

In his very specific approach of the gold markets, Eric has built a substantial international audience for his site and letter. His Gold Discovery Premium service offers investors the possibility to subscribe to the special Member Section of his site.



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