

THE LAST LAUGH?

(EDITORIAL FOR THE KITCO.COM "CONTRIBUTORS CORNER")

Gold and silver staged quite a comeback as 2006 came to a close. Enough of a comeback for a lot of naysayers to sidle over to gold and silver at year end and predict a good year for precious metals in 2007.

No sooner did that happen then both gold and silver both got taken out behind the woodshed. What happened? The same forces that have dogged precious metals in the past reasserted themselves as soon as the New Year began. Oil prices, which had been struggling in the \$60 to \$65 range suddenly and rapidly fell over seven dollars in three sessions. At the same time, the Dollar staged a minor comeback. We've inserted a US Dollar Index 12 month chart below which gives some perspective. The Dollar has been climbing since the start of December on the back of slightly stronger economic numbers, but its hardly rocketing upward. It's barely though its 50 day MA and well below the 200 day.

We've been less bearish on the US than many gold followers so we were not surprised at those numbers. In fact, gold held its own against the Dollar through December and only dropped once we entered 2007. Coincidence? We think not. The real start of the drop was January profit taking, pure and simple. It's a common occurrence. It might surprise some short term bulls because it was largely absent the past couple of years but this is how the market for metals and especially metal exploration stocks often looks in early January. Traders have profits they don't want to book until the next tax year and funds have profits they want to show as being on the books at year end (so they can crow about them) and hold off on selling or profit taking until January. The profit taking was exacerbated in this case by some "good" news on the economic front that goosed the dollar and pulled the bids out from under metals.



The good news in this case was a strong employment number for November. It put the scare into traders who had just finished reading the Fed minutes which left no doubt that the Fed Open Market committee was still worried about inflation. The effect of both these items would have been more muted if not for the strong wage gains for November that were part of the employment report. Wage gains of 0.5% for the month and 4.2% year over year. That's good news for employees but anathema for the bond market. As we've told our readers many times in the past two years, wage inflation is what really needs to be watched. For all the moaning and wailing about high commodity prices they do not form a large enough portion of the economy to push inflation up on their own. The one cost input that can do that is wages.

We're hardly panicking, since we know the full impact of the housing slump will take months to unfold. It's quite possible those employment gains will get reversed by summer. Likewise, we're not assuming the worst yet in terms of interest rates, though we think the Fed will stand pat for a couple of meetings at least. In short this is the sort of knee jerk, margin call, stop loss induced short term plunge we see from time to time in the metals market. We think gold and silver will be among the top performers again this year. The start of year weakness should be viewed for what it is; a chance for those bold enough to buy low and sell high to position themselves for future profits.

David Coffin and Eric Coffin are the editors of the HRA Journal, HRA Dispatch and HRA Special Delivery publications focused on metals exploration, development and production stocks. They were among the first to draw attention to the current commodities super cycle and have generated one of the best track records in the business thanks to decades of experience and contacts throughout the industry that help them get the story to their readers first. Please visit their website at www.hardrockanalyst.com for more information.

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