

Silver Surges but Remains Undervalued Vis-à-Vis Gold

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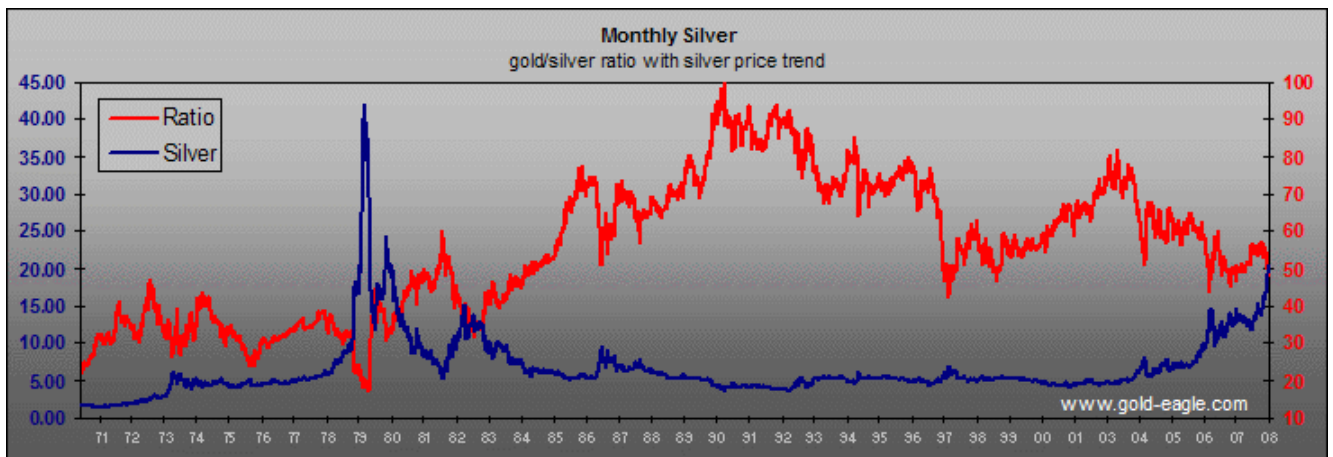
Gold fell some 1.5% last week as investors took profits with gold having been up some 10% in the previous three 3 weeks. But the short and medium term prospects look sound in the light of strong fundamentals and some important indicators - silver was up by another 4.2% last week and the gold mining indices were also higher (XAU +4.6% and HUI +2.3%). The mining indices are often a leading indicator and silver usually underperforms gold in the early stages of rallies and outperforms in the latter. Silver's recent strength (up by some 15% since the start of the year) may be a prelude to higher gold prices in the coming weeks.

<i>09-Feb-09</i>	<i>Last</i>	<i>1 Month</i>	<i>YTD</i>	<i>1 Year</i>	<i>5 Year</i>
Gold \$	904.62	6.04%	2.78%	-1.97%	122.43%
Silver	12.99	15.65%	14.93%	-24.36%	102.93%
Oil	40.30	-1.29%	-9.64%	-56.05%	22.75%
FTSE	4,280	-3.79%	-3.48%	-26.01%	-3.49%
Nikkei	7,969	-9.82%	-10.05%	-38.78%	-23.39%
S&P 500	869	-2.44%	-3.83%	-34.75%	-23.79%
ISEQ	2,456	-8.58%	4.79%	-62.44%	-52.41%
EUR/USD	1.2936	-3.99%	-7.42%	-10.81%	1.95%

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The recent sharp rally in the US dollar appears unsustainable and the USD Index was down 0.64% last week and US bonds also fell again - the 10-Year bond sold off again and the yield rose another 4.75% (from 2.9% to 2.979%). As ever, the bond market remains of fundamental importance and nervousness about the humongous size of the Obama bailout and stimulus packages and talk of central banks printing money to buy government bonds is not helping sentiment here. And government debt issuance is set to surge in the coming weeks and there is a real concern that there simply will not be enough buyers - meaning that bond prices may fall from their lofty heights and long term yields and interest rates begin to rise again.

The gold/silver ratio has fallen to around 70 (\$905oz/\$13/oz = 69.6) today from around 80 in mid January. The long term historical average is 15:1 and this is because it is estimated that geologically there are some 15 parts of silver in the ground for every one part of gold. It is important to note that silver, unlike gold, besides being a safe haven investment is also used in industry and it is believed that since the dawn of the industrial revolution some 95% of the world's silver has been used up in industrial applications. Because of gold's much higher value, it gets recycled and all the gold mined in the world ever is still with us but photography and other industrial uses makes silver like oil - when used it is gone forever.



The 1970s saw an average gold to silver ratio of around 25:1 and fell below 20:1 when silver rose to over \$45/oz nominally. Thus it seems very likely that in the coming years, silver may well return to its long term historical average of closer to 15:1. This means that silver is likely to continue to outperform even gold in the coming weeks and months. Silver may return to its recent highs of over \$20/oz in 2009 due to very strong supply demand fundamentals. It is also important to note that the CFTC investigation into artificial manipulation and suppression of the silver market could potentially lead to a massive short squeeze.

All investors should diversify within the precious metals allocation in their portfolio and own silver as well as gold. Gold remains the ultimate safe haven while silver is a safe haven but has the potential for very significant returns and growing wealth in the coming months.