



Karvy Comtrade Ltd.

Precious Metals Outlook Q4 2010

Recommendations

COMEX Gold (\$/oz)	Buy at 1260 - 1280 TP 1370 SL 1210
MCX Gold (₹/10gm)	Buy at 18500 - 18700 TP 19500 - 19700 SL 18000
COMEX Silver (\$/oz)	Buy at 20.50 - 20.70 TP 22.50 then 23.50 SL 19.00
MCX Silver (₹/kg)	Buy at 31600 - 31800 TP 34600 SL 29100

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Economic Backdrop

The global economic recovery, which came to a halt in the first half of this year in the wake of European sovereign crisis, is now proceeding although at different speed. Developed countries are facing a lukewarm recovery, given high unemployment and rising public debt.

The world's largest economy, the U.S., is recovering after the global economic crisis, but fear factor still prevails as weak housing markets, high unemployment, and huge public debts remain a major cause of concern. Growth is resuming although at the lower pace but the country faces severe challenges of bringing its debt to more sustainable levels without jeopardizing the recovery. The IMF forecasts U.S. economic growth of just over 3 ¼ percent in 2010 and about 3 percent in 2011, with inflation very low and unemployment remaining above 9 percent. The U.S. GDP growth, on Q/Q basis, slowed down to 1.60% (annualized) in 2Q 2010 over the first quarter growth of 2.40%. Unemployment rate elevated to 9.6% in August as a result of continued joblessness in July and August month. However, President Obama has announced additional steps to grow the economy and create jobs, including a US\$50 billion transport infrastructure plan. Industrial production is also not showing a steady growth as the same rose 1% in July and 0.20% in August. Housing sector is another big headache for the government agencies, which is finding difficult to revive. Slowing economic recovery as a result of high unemployment and low income levels also hampers demand for housing in the country. New home sales declined more than 16% to 276,000 units, alongwith existing home sales also falling by 29% to 3.83 million units in July. Housing starts and building permits also took a dip, showing weakening demand for houses in the future. Although housing reports came slightly positive for August month.

Apart from these issues, the next challenge for the United States is the size of its public debt. U.S. publicly held debt has been rising at a rapid pace since the onset of the financial crisis and is currently floating above 60% of GDP, taking total debt to approximately 93% of GDP, as of July 2010. Interestingly, publicly held debt was hovering at 36% of GDP in 2007. In spite of stabilizing its public debt, the President's recent budget proposal also estimated continuing deficit throughout the next decade. This will push net debt to 90% of GDP by 2020. Rising public debt will weaken eminence of the U.S. dollar in international markets. In order to halve budget deficit by 2013 and stabilize public debt at just over 70% of GDP by 2015, the Federal government needs to cut back on spending and increase revenues. The decision by the central bank to keep its interest rates at a historic low (0.25%) is appropriate as low interest rates lessen the burden of interest liability of the government. U.S. economic recovery is expected to remain fragile even for the next quarter as well.

On the other hand, eurozone's weak and uneven economic recovery came on track with the region having grown at 1% in the second quarter against first quarter growth of 0.3%. Evidence also mounted that the three months to September would also see stronger growth than originally forecasts, according to Jean-Claude Trichet, ECB president. Signs that the eurozone is over the worst of the crisis, which earlier this year threatened the stability of Europe's 11-year-old monetary union, have boosted confidence in financial markets.

The 16-nations bloc experienced some relaxing signs in the Q3 2010 after sovereign risks prevailed during the first two quarters of this year. Euro-zone debt concerns eased in the third quarter as a result of cumulative efforts taken by respective governments and the European Central Bank. Debt-laden Greece was praised by European Union and the IMF for its progress in implementing its emergency economic rescue programme. Major challenge remains with high unemployment which is still lingering at 10% in the eurozone and that seems to be a detrimental to the region's economic recovery. However, macroeconomic policies and extraordinary measures regarding cut in government spending to bring down debt levels will support the upswing. Interest rates are prevailing at record low levels of 1%. During the quarter, eurozone carried out stress test to check the resilience levels of its financial system, which turned out to be quite satisfactory. Stress test results showed that only 7 banks may not be able to cope with adverse scenario and thereby, they would see their Tier 1 capital ratio fall below the threshold limit of 6%, meaning that they will have to raise more capital.

Last but not the least, Asian economies continued to lead the global economy, thanks to relatively larger domestic demand bases in India, China and Indonesia. Interest rates have now started rising in the region amid economies growing at a rapid pace. India increased its benchmark interest rates twice in the third quarter to cool off inflation primarily but it was also envisaged that domestic economic growth supports these hikes in interest rates. India's second quarter GDP expanded at 8.8% as compared to 8.6% growth in the corresponding quarter of the last year. Inflation also lowered to 9.5% in August from above 10.5% in June-ending second quarter. Factory output also rose better-than-expected with clocking 13.8% growth in July from a year ago period. Overall, domestic economic sentiments were buoyant with the country's benchmark index heading for 21K for the first time in nearly 30-month period. India's regional partner China was worried on its economy getting overheated. Chinese inflation rose to 3.3% in July compared to 2.9% during the same month last year. The PMI manufacturing indicator advanced to 51.7 in August from 51.2 in the month before. The dragon seems to have implemented some tightening measure in the recent past to cool off the economic overheating and as a result, Chinese real GDP grew at 10.3% in Q2 from a year ago, down from an annual gain of 11.9% in Q1. However, China's industrial production rose 13.9% in August from a year ago, better than expected. China also allowed limited fluctuation in its currency amid growing pressure to revalue its currency. Another Asian giant which is also the only developed economy in Asia, Japan, came across different situations where notable appreciation in its domestic currency, the yen, turned out to be major headache for the authorities. The Yen's appreciation became crucial issue for the government as it hampers export-led recovery. Eventually, the government had to intervene for the first time in six years by selling ¥2 trillion in the market. However, analysts say that the resultant effect may not be long-lasting.

Overall, the global economic outlook remains uncertain with recent macroeconomic indicators posting to a slowdown in the pace of the world economy's recovery. It is still not clear if the loss of momentum in the global economy is temporary or it signals a greater underlying weakness in private demand as policy stimulus winds down. However, in contrast to many developed economies which are struggling to maintain economic momentum, emerging economies will continue to grow strongly. Developed economies are likely to continue with their loose monetary policies for an extended period of time to spur

their domestic economic growth. These economies are expected to grow at 2.6% in 2010, as per IMF projections. As the economic recovery takes hold or becomes weak, fiscal policies need to remain supportive of economic activity in the near term, and the fiscal stimulus planned for 2010 should be implemented fully. In fact, major economies felt the need of injecting more stimuli to prop up their domestic economic growth. Recently, there have been speculations that U.S. will buy bonds worth of as much as \$1 trillion to spur the domestic economic growth. However, given growing concerns about fiscal sustainability, countries should also make progress in devising and communicating exit strategies.

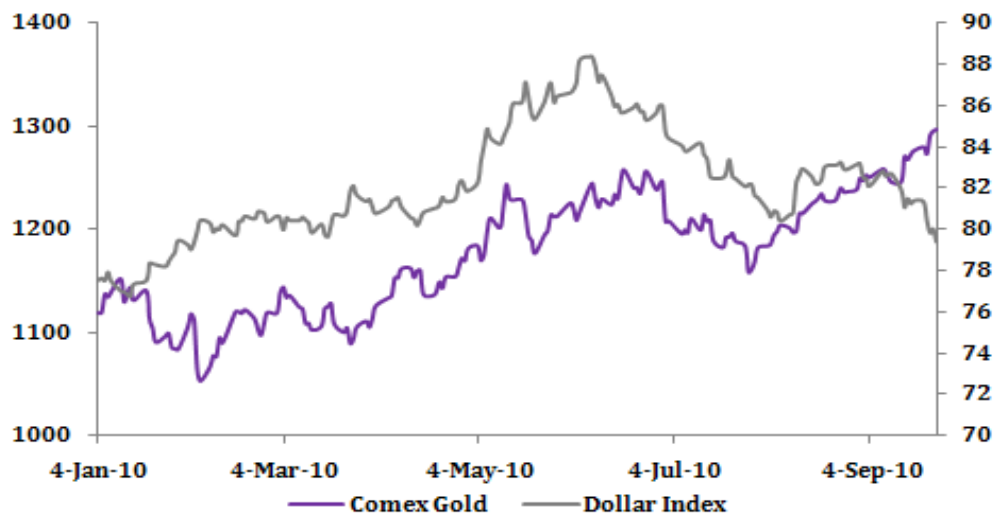
Gold: Price Movement

After its breakthrough to the then new high point during the end of second quarter, gold rallied to new highs in the third quarter of 2010. The yellow metal gave up some grounds in July after reaching peak in June-end, which it later recovered in subsequent months i.e. August and September. September's reputation as gold's favorite month remains intact as the metal making new highs in September and sustaining those gains. During the quarter, COMEX spot gold traded on an average price of above \$1222/oz. Spot gold traded in the range of \$1157.03 - \$1313.45/oz during the quarter.

Gold's gains were mainly imparted by weak dollar and uncertain economic conditions which prevailed during the whole quarter. Weaker dollar spurred gold's alternative investment demand while concerns of faltering economic recovery strengthened the yellow metal's safe haven appeal. The dollar index fell more than 7.5% during the quarter while gold rose more than 4%. Recently, both gold and the dollar resumed their classical inverse relationship after having traded in same tandem in this year.

Apart from lowering dollar index, strong **investment demand** was another major reason which took prices to new highs during the quarter. Investment demand was mainly led by ETF demand. Though SPDR, the world's largest gold ETF, didn't add much to its holdings, but total exchange-traded gold holdings rose to 1617.84 MT as on Sep 24, 2010.

Exhibit 1: COMEX Gold and Dollar Index



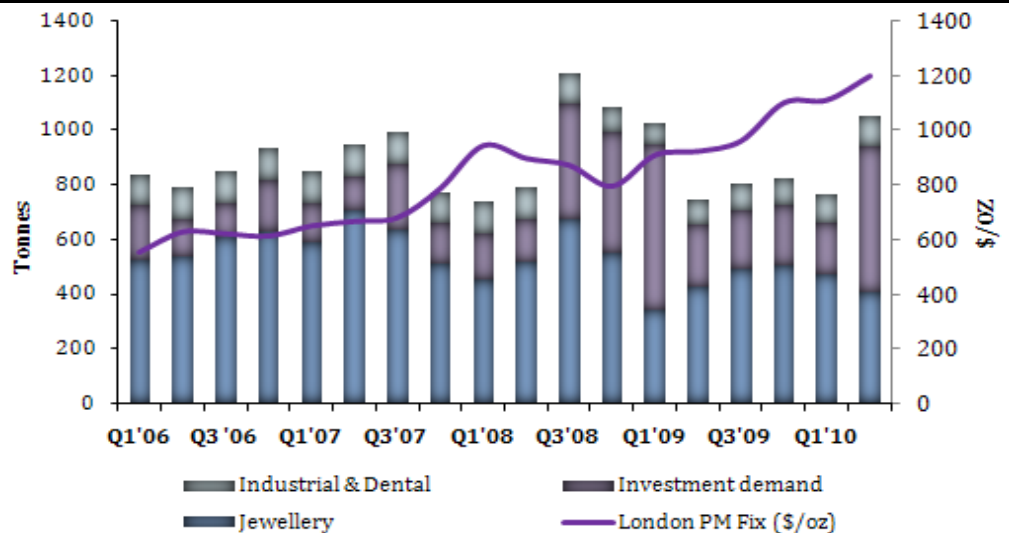
Source: Bloomberg & KCTL Research

CFTC reports suggest rising long positions in gold futures on COMEX after having declined in the beginning of the Q3 2010. Non-commercial holders, mainly speculators, added more than 6500 fresh long positions during the quarter ended on Sep 21, 2010. The Q3 2010 saw net long positions declining in July followed by speculators betting on the yellow metal in the later part of the quarter, taking net long positions to the level seen at the end of the last quarter. Total net long positions stood at 244,013 contracts as on Sep 21, 2010 from 209,042 contracts in the beginning of the Q3 2010. A recovery in net long positions after having declined in the beginning can be attributed to firm bullion prices during the quarter. On the other hand, commercial holders (hedgers) deliberately reduced their both long and short positions in gold during the quarter.

Demand

Total gold demand in Q2 2010 rose 38% to 1047 tonnes, largely due to strong investment demand which saw a manifold increase from the previous quarter and the same quarter last year. ETF-led demand made significant contribution to overall increase in investment demand, which grew by 414% to 291 tonnes from 57 tonnes in the corresponding quarter last year. Despite surging bullion prices, traditional jewellery demand remained robust with consumption of 406 tonnes of gold in Q2 2010, just 4% below year-earlier levels. With the return of demand for consumer electronics, industrial demand grew by 14% to 107 tonnes in Q2 2010, compared to Q2 2009. The world's largest gold consumer, India, saw a little change from year-earlier levels, down just 2% at 123 tonnes, according to the World Gold Council. Similarly, China saw demand for gold jewellery increase by 5% to 75.4 tonnes.

Exhibit 2: World Gold Demand



Source: World Gold Council & KCTL Research

The World Gold Council expects India and China to provide main thrust of overall growth in demand, particularly for gold jewelry, for the remainder of 2010. Retail investment will continue to be a substantial source of gold demand in Europe. Electronics demand is likely to return to higher historic levels after the sector exhibited further signs of recovery, especially

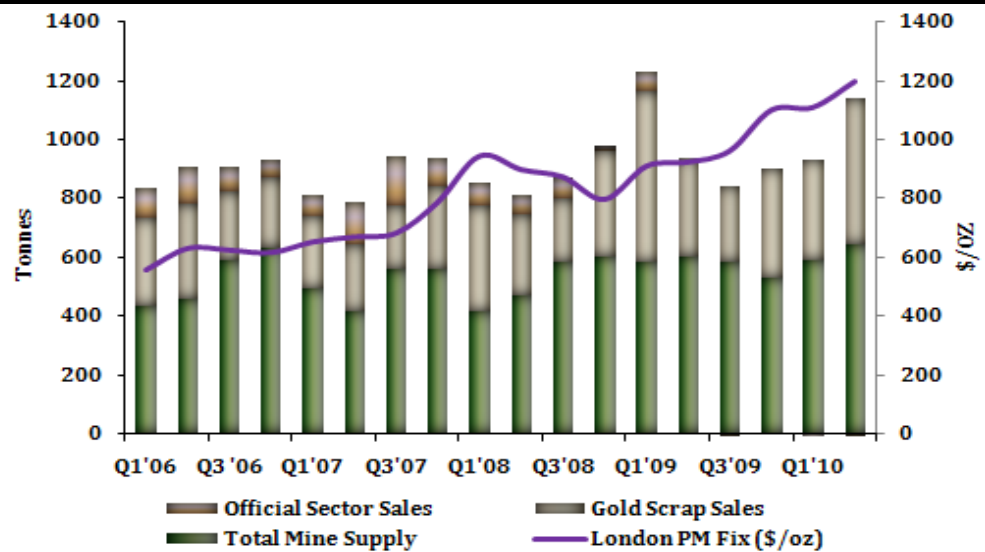
in the US and Japan. Investment demand is also likely to remain firm amidst prevailing economic uncertainty and investors resorting to gold as a safe haven asset class.

Supply

Total supply of gold in the second quarter totalled 1132 tonnes, a rise of over 21% from the second quarter of 2009. Mine supply increased 4% to 659 tonnes from 633 tonnes in the same period a year earlier as a raft of new operations or ramped up existing productions. Rising bullion prices tempted miners to increase the supply. Australian production contributed the bulk of the increase in output as Newmont's Boddington mine completed its first year of production. Further positive contributions came from Mexico, where Agnico Eagle ramped up its Pinos Altos operation, and Argentina, with Barrick's expansion of its Valadero mine.

Recycling activities (old gold sales) were another major reason of increased supply in the market, in the lieu of high price environment. Old gold sales rose more than 45% to 496 tonnes from 338 tonnes in second quarter a year earlier. It was evident that the bulk of scrap supply came from non-western markets, notably the Middle Eastern and East Asian markets.

Exhibit 3: World Gold Supply



Source: World Gold Council & KCTL Research

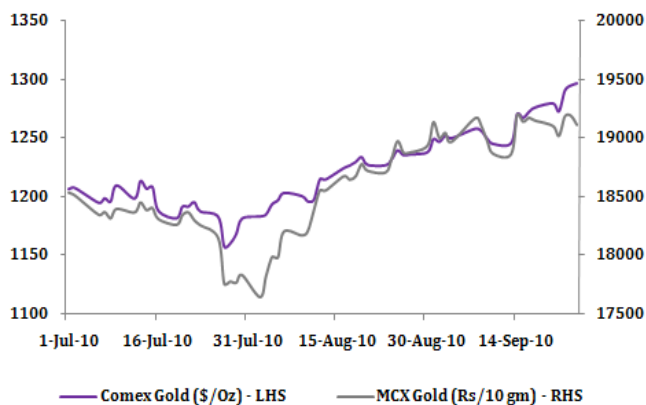
On the supply side, jubilant bullion prices are expected to keep miners' morale higher which will induce them to increase mine supply. However, official sector will continue to be responsible for taking supply out of the market, as central banks becoming net buyers of gold. The IMF has made a sale of 283.1 tonnes so far till Q2 2010, still leaving 120.2 tonnes remaining of the total 403.3 tonnes earmarked for sale.

Gold in Different currencies

Strong gold price were seen sustaining their YTD gains across key currencies. Gold prices were upbeat in the dollar and rupee terms throughout the quarter but took a dip in other major currencies during the quarter. However, prices recovered some of their lost grounds towards the end of the third quarter. The first half of this year witnessed a considerable appreciation in gold and dollar on account of both attracting safe haven demand. Later, the constituent currencies like; euro, yen, pound etc of the dollar index strengthened against the dollar which led the bullion prices to take a correction in these currencies.

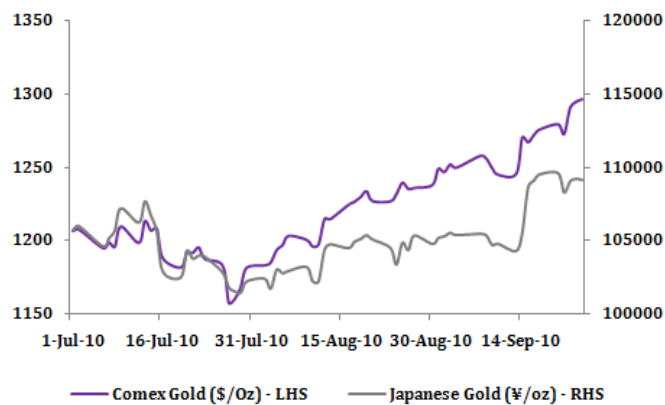
During the quarter, U.S. dollar-priced and rupee-priced gold rose more than 4% and 1.35%, respectively. In the six elementary currencies of the dollar index, bullion prices fell as the yellow metal moves inversely to the currency appreciation. Yen-priced gold corrected by 1% while US gold rose over 4% during the third quarter. The yen strengthened by nearly 5% against the U.S. dollar. US gold outperformed gold prices in the euro and pound terms also as both the currencies appreciated by over 10% and 6%, respectively against the U.S. dollar. Other constituent currencies of the dollar index also corrected against the U.S. dollar with Swedish Krona gained the most by nearly 13%.

Exhibit 4: Dollar-priced Gold & Rupee-priced Gold



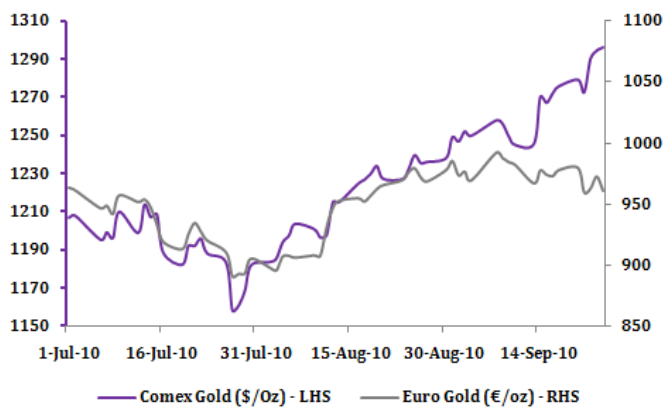
Source: Bloomberg & KCTL Research

Exhibit 5: Dollar-priced Gold & Yen-priced Gold



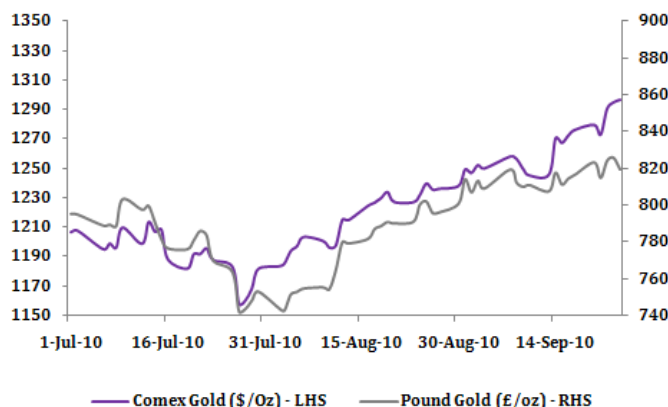
Source: Bloomberg & KCTL Research

Exhibit 6: Dollar-priced Gold & Euro-priced Gold



Source: Bloomberg & KCTL Research

Exhibit 7: Dollar-priced Gold & Pound-priced Gold



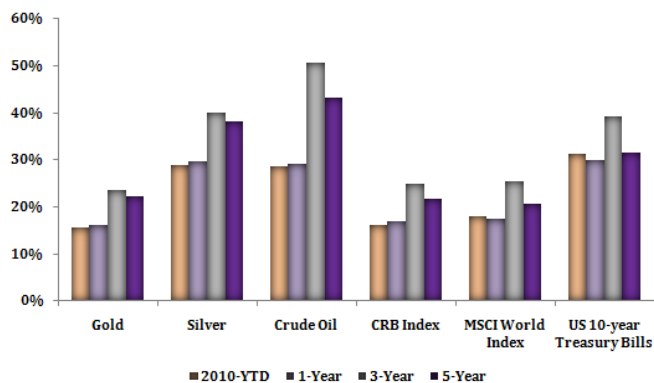
Source: Bloomberg & KCTL Research

Volatility & Co-relation

With uncertainty, volatility and inflation being the order of the day, one asset is the clear winner when it comes to protecting wealth. Gold has historically been found substantially less volatile than other assets mainly; equities. In the current year till date, the volatility of the MSCI World index for stocks has been nearly 18% (annualized), whereas that of gold has been below 16%. The U.S. treasuries, which are known as safer investments, witnessed over 30% volatility this year till date. The volatility of gold has been lower than that of oil, other precious metals, the CRB commodity index and the most equity indices in the past.

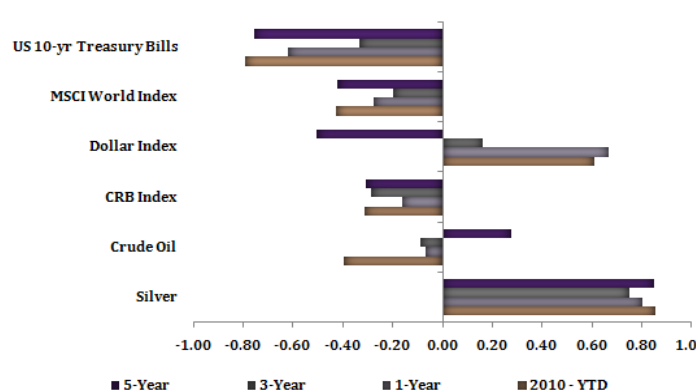
Gold has also negative co-relation with major asset classes which makes this precious metal move independently. Over the past five years, gold moved inversely to the U.S. treasuries and MSCI World Index. Global equities have fallen by more than 13% over the five year period ended on Sep 24, whereas gold has risen stunningly during the same period. In 2010 till date, co-relation numbers deviated from their historical patterns. Gold and the dollar index, which generally move inversely, shifted to positive co-relation as both of them advanced on safe-haven demand. Another fact lies with gold and crude oil which moved inversely in this year against their historically proved positive co-relation. Prevailing economic worries, which spurred gold's safe haven demand but made crude oil prices weaker, could be attributed to such break-ups.

Exhibit 8: Gold is less volatile



Source: Bloomberg & KCTL Research

Exhibit 9: Co-relation



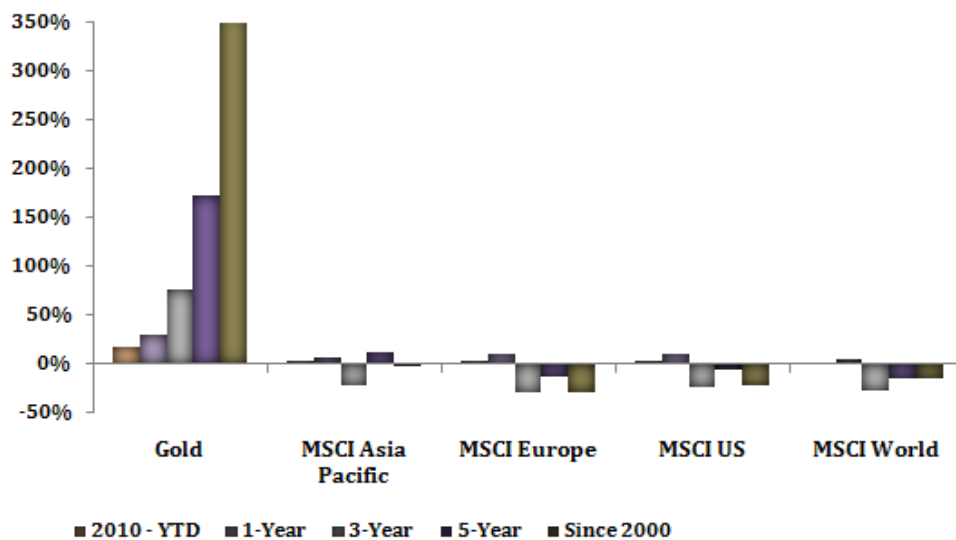
Source: Bloomberg & KCTL Research

Gold and Equity Markets

Global economic uncertainties lowered the appeal of equities as stock markets didn't do fairly well amid such doubtful economic conditions. The poor performance of the equity markets since 2000 has driven many investors to look beyond traditional assets. Gold's strong performance, during this period, has stirred up their interests. Since 2000, the yellow metal has risen nearly 350% against negative returns of equities across regions. Gold has outperformed equities this year also till date with a return of more than 18% against average gains of 0.09% in the MSCI World index for stocks.

For 1-year ending September 2010, gold prices have surged nearly 29% while global equities rose merely 3.4%. On 3-year, 5-year and since-2000 horizon, equities have plummeted while gold prices have skyrocketed.

Exhibit 10: Gold outperforms equities



Source: Bloomberg & KCTL Research

Gold & Bond: Inter-market analysis

There is an inter-market relationship between gold and bonds which may not be evident at first glance. The reason why the two disparate markets are connected is that they both track one common factor: inflation or expectation of future inflation. For this reason, they tend to dance around each other.

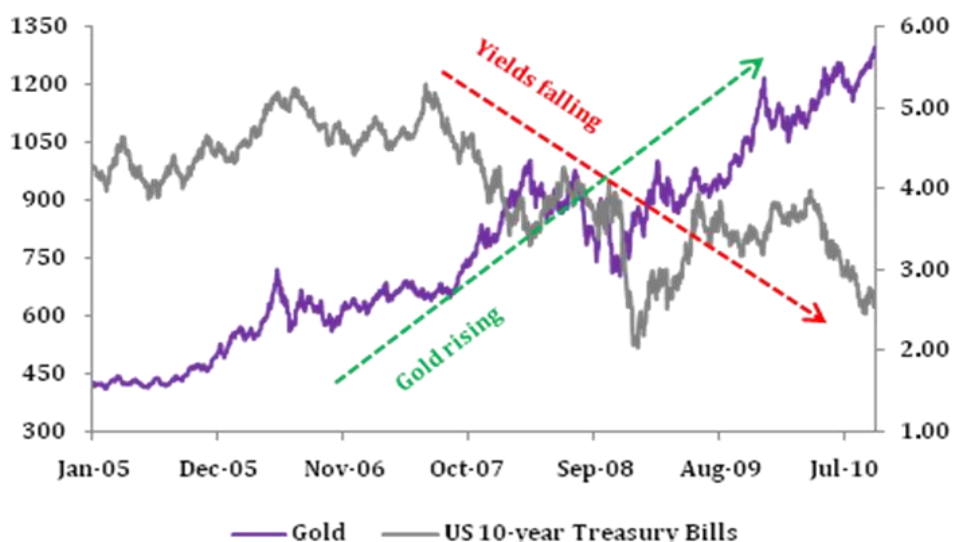
When the market expects future inflation to be higher, gold prices rise and bond prices fall (yields rise). So in effect, by watching one market, we can gain insight into the other.

Gold is always considered as a guard against inflation, and inflation is very bad for the holder of the govt. bond, hence bond price should fall and thereby yield on the bond should increase. However, it may not exist as other factors are in force. We don't find any meaningful relationship between them and they both have gone their separate ways.

Since inflation expectations have come down, governments are keeping their respective benchmark interest rates lower which in turn decreases the yield on treasuries i.e. higher bond prices. Currently, yields are hovering at near historical low levels while gold prices are soaring which means they are telling two different stories as they did in 2007-08. From July 2007 to March 2008, gold prices rose and treasuries' yields dropped. It was because of credit and interest rate risks. Expectations were growing for the fed to lower interest rates in response to the housing and credit crisis. Another example is when in 1980 gold was ruling at all time high in real term (inflation-adjusted), the ten year Treasury yield was 10.8%. But recently when gold is trading close to \$1300/oz, the yield on ten years T bonds was just 2.6%. This is near to historically low.

So why is this current situation? We expect performance of gold and T bonds negatively correlated or we can say that yield and gold price should be positively correlated. Here, the threat of inflation—at least in the near term—has diminished. This suggests that gold is more of a hedge against financial stress than a hedge against inflation. The source of this stress could be inflation, deflation, currency devaluation or major upheavals in the economic and political arena.

Exhibit 11: Gold & Bonds

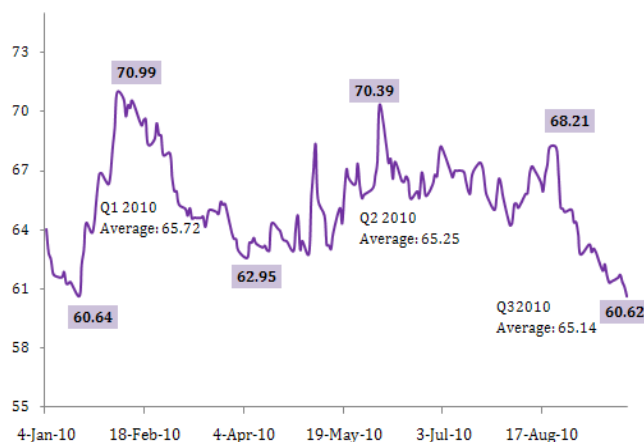


Source: Bloomberg & KCTL Research

Gold/Silver Ratio

The average gold/silver ratio was little changed during the quarter and decreased to 65.14 from 65.25 in the previous quarter. Overall, the ratio traded lower as more upside was witnessed in silver in comparison with gold. Silver jumped nearly 15% while gold saw moderate gains of over 4% during the quarter. Gold was mostly seen trading above \$1200/oz levels.

Exhibit 12: Gold/Silver Ratio



Source: Bloomberg & KCTL Research

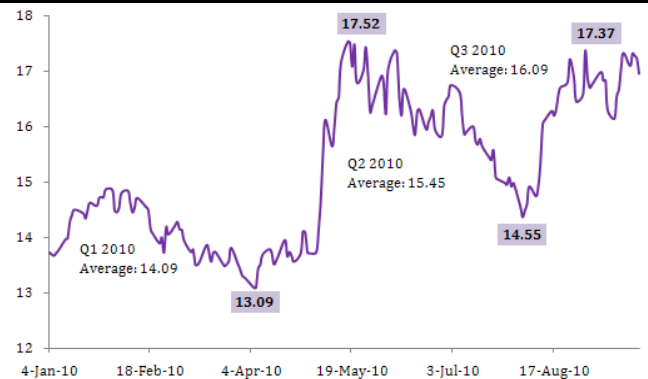
This year, the ratio had been averaging at around 65 levels.

If silver trades at an average price of US\$19.80/oz, then applying the average ratio of 65 takes average gold prices to US\$1,287/oz during the next quarter.

Gold/Crude Ratio

The historical positive correlation between gold and crude oil remained weak in this year. The current year 2010 saw a continued break-up where both crude oil and gold parted their ways since the end of the first quarter. The second and third quarter of the year 2010 experienced European debt crisis and uncertain economic conditions which sent crude oil prices lower while the same lifted the bullion prices as a safe haven investment during this period.

Exhibit 13: Gold/Crude Ratio



Source: Bloomberg & KCTL Research

Average gold/crude ratio rose for the second quarter in a row and was seen hovering at above 16 levels against 15.45 in Q2 2010. The ratio was seen trading at an average of 14.09 in Q1 2010. The reason behind the rise in ratio in third quarter could be attributed to fall in crude oil prices while a surge in bullion prices. Average crude oil prices dropped nearly 2.5% while average bullion prices rose more than 2% in third quarter over the second quarter.

Decoupling between these two commodities is likely to continue for some more time in the near future. The ratio may widen further before consolidating towards year-end. If we expect crude oil to trade at an average price of US\$75/barrel during the next quarter (Q4 2010), then applying the expected ratio of 17 implies average gold price level of nearly US\$1,275/oz.

Trade cautious

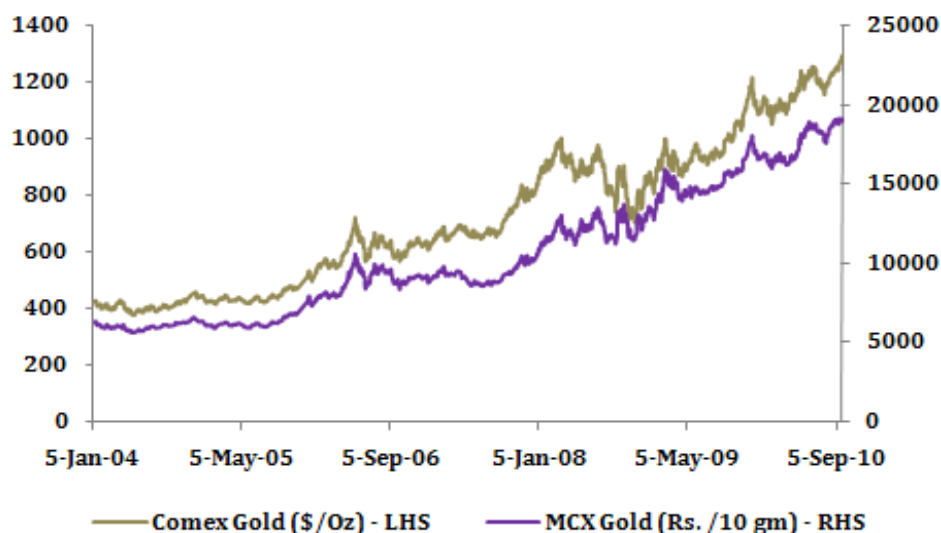
In the nutshell, gold is well positioned with further gains after its recent break of the psychologically important \$1300/oz levels. However, some profit booking may kick in which will do for a short period and then gold's upward momentum will continue again. Going by the past patterns, October may see a correction and then a second surge in prices is expected in November and December. Disappointing economic news will continue to drive it through. Talks of the Fed's announcement that quantitative easing, which may begin as early as in November, will further push bullion prices higher.

Although gold looks firm even in the next quarter, Indian gold may be restrained by rupee appreciation as it has happened repeatedly during the quarter. COMEX gold has made a string of new highs in the last few weeks but MCX gold futures failed to match up with that performance. Rupee has appreciated by more than 2.5% to 45.2550/USD as on Sep 24, 2010. Indian rupee traded in the range of 46-47 during most of the quarter; however, deviating from the range in September only when rupee gained little less than 4% and

thereby, disturbing the parity prices in India. COMEX gold gained over 4% during the quarter while MCX gold rose merely 1.5%.

We expect rupee to continue to be major hindrance in bullion's upside on MCX trading desk, despite having firm view for COMEX gold prices.

Exhibit 14: Comex Gold & MCX Gold



Source: Bloomberg & KCTL Research

Technical Analysis

Gold continued to glitter for the fifth consecutive quarter and rose more than 4% during the quarter. Gold has breached the crucial resistance of \$1285/oz on monthly chart.

Pattern study: The next crucial resistance to watch is \$1365 levels which is a full length target of the *"Inverted head & Shoulder"* pattern, making a break out on higher side at \$990 levels in the month of September 2009.

Gold is witnessing *"Trend Channel"* formation on the upper side of the monthly chart also suggesting bullish view for the next quarter.

The closing of the Quarterly candle has made a *"Hanging Man"* pattern which suggests the trend reversal.

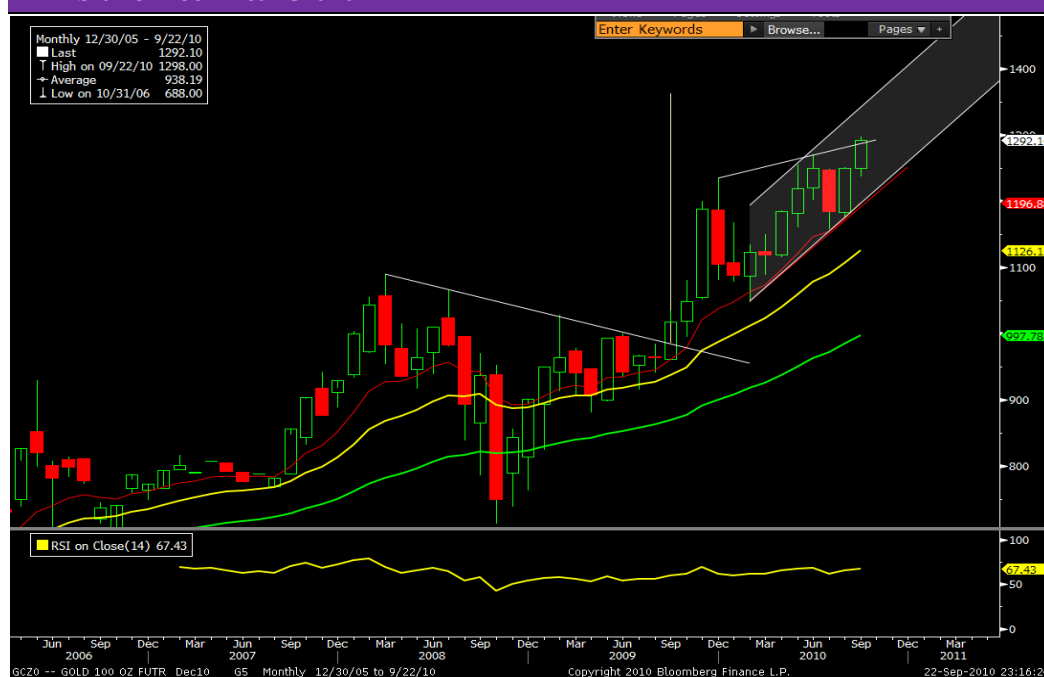
Momentum indicator study: The momentum indicator RSI (14) is trading at 0.847, falling in over-bought zone but still indicating further bullish trend for the coming quarter and also supporting the prices with a RSI positive divergence. The short term EMA's (9, 18) and medium term EMA (45) are also suggesting further upside as the market is trading well above them. Another momentum indicator "Stochastic" suggests prices to trade higher as the K% and D% are trading at 0.989 and 0.857, respectively with making no sign of overlapping and turnover on down side. Volumes have declined from 4.217M to 2.948M over the last quarter.

Quarterly Pivot Analysis

Exhibit 15: Pivot Table

Exchange	Support 2	Support 1	Pivot	Resistance 1	Resistance 2
COMEX	1108.60	1208.50	1259.20	1359.10	1409.80
MCX	17210	18165	18711	19666	20212

Exhibit 16: Technical Chart



Source: Bloomberg & KCTL Research

Elliot Wave Analysis

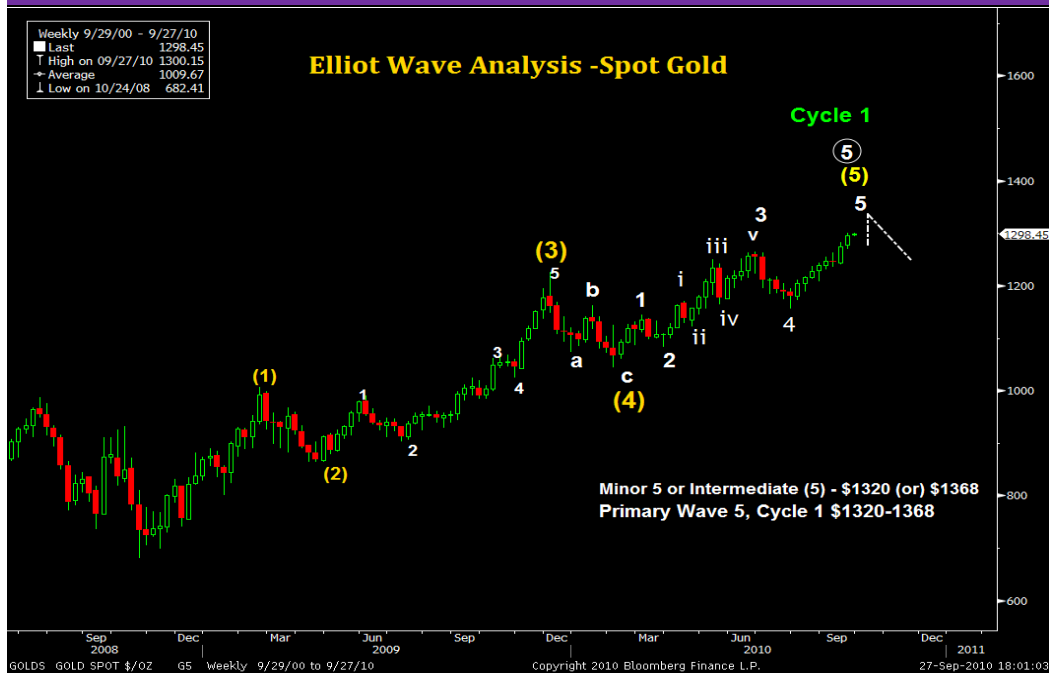
View: Upside

Strategy: Buy for short term, Sell for long term

Recent wave: Minor wave 5 of intermediate wave (5) of primary wave 5 of Cycle 1 is in progress, which is likely to terminate around 1320 or it can extend till 1368 levels.

We expected minor wave 3 of intermediate (5) to terminate at \$1266 levels in last quarter; fortunately market made a high of \$1265.3 (end of minor wave 3). Later it took correction till \$1157.03 levels, described as minor wave 4. Hereafter, market started rising and is currently at \$1298 as minor 5 of intermediate 5 of primary wave 5 is expected to end around \$1320 or it can extend till \$1368 levels. On downside, key level to watch is at \$1265.30 levels; sustaining above this level may result in to prolong its fifth wave extension. Only a closing below \$1265 confirms the end of bullish trend and is expected to be in correction phase. Overall, we expect prices to remain higher if market holds the support at \$1265.

Exhibit 17: Elliot Wave Chart



Source: Bloomberg & KCTL Research

Exhibit 18: Recommendations

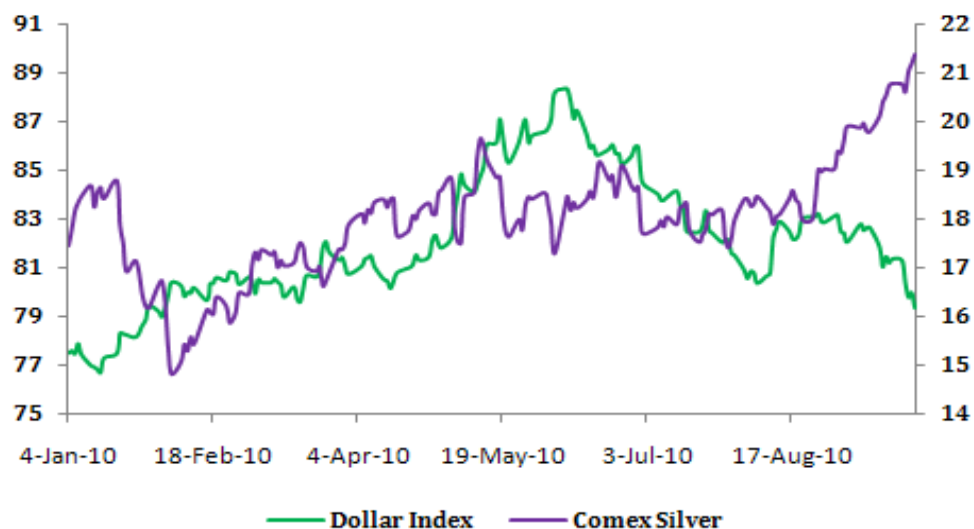
COMEX (\$/oz)	Buy at 1260 - 1280 Targeting 1370 Stop Loss 1210
MCX (₹/10gm)	Buy at 18500 - 18700 Targeting 19500 - 19700 Stop Loss 18000

Silver

After being trapped in a trading range between \$17.5/oz and \$18.5/oz during most of the quarter, silver has broken out to the upside and in less than three weeks, prices first hit \$20/oz and then \$21.40/oz, the level last seen 30 years back. Silver prices moved from \$18.67/oz last quarter to a hair below \$21.40/oz on Sep 24. This is an increase of nearly 15%! Not bad if you have been long, too bad if you have been short.

However, there was not much increase in average silver prices during the quarter as prices traded on an average of \$18.75/oz against an average of \$18.38/oz in the last quarter. Silver mainly rode the coattails of gold's success as weak economic conditions made precious metals a hot investment avenue. Weaker dollar could mainly be attributed to gains in precious metals.

Exhibit 19: Silver & Dollar Index



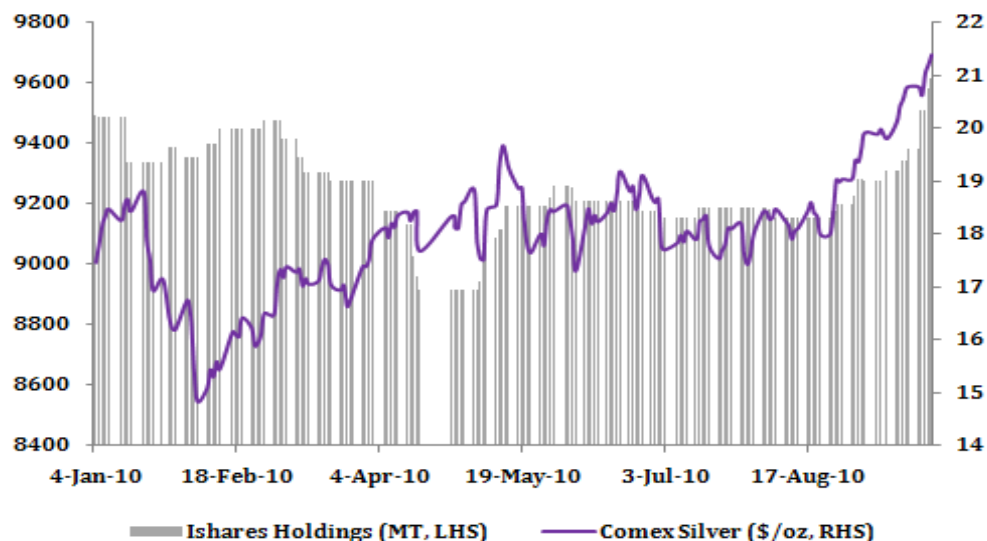
Source: Bloomberg & KCTL Research

Silver, gold's poor cousin, has closely tracked bullion prices higher. Both silver and gold have historically stood the test of time, as a medium of exchange, a store of value and a safe haven in times of turmoil. These two have historically moved in same tandem, although silver showed more volatility in either direction. Nowadays, silver is taking investors' precedence over gold, shown by the popular Gold/Silver Ratio (GSR) which broke downwards. The Exhibit 14 above shows that falling Gold/Silver Ratio means silver has been perhaps more in demand, mainly investment demand. It was primarily because of silver being a cheaper alternative to the yellow metal which benefitted this white metal to take big moves in the recent times.

Silver's investment demand grew like anything in the third quarter against a decline in the penultimate two quarters of this year. Ishares Silver Trust, the world's biggest silver-ETF, witnessed a cumulative decline of nearly 316 MT in its holdings in the first half of this year against a rise of 436 MT in the Q3 2010. This was a rise of a little less 5% that could be attributed as one of main reasons in silver's upside of nearly 15% during the quarter.

This surge in investment demand for silver signifies a resurgence of the importance of silver as a store of value.

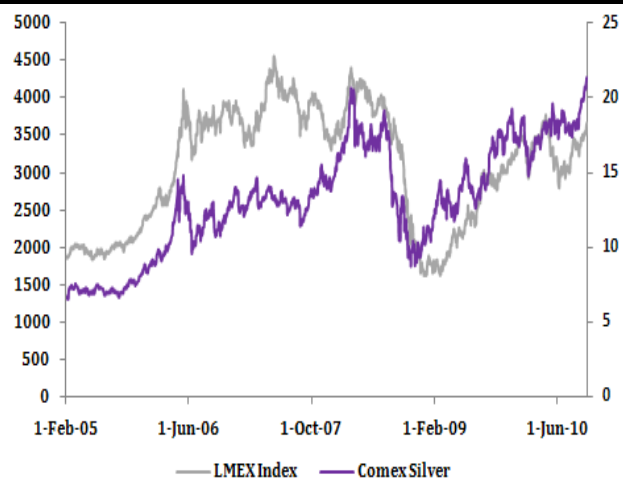
Exhibit 20: Ishares' Silver Holdings & Silver Prices



Source: Bloomberg & KCTL Research

Apart from precious metals; mainly gold, silver also tracks base metals because of silver's growing usage in industrial applications. Silver is closely tied to economic activities. Silver is also a by-product or co-product of base metal mining. Out of total silver demand, more than 35% demand occurs from industrial sector which makes this white metal an industrial metal. Although silver has not shared a very strong co-relation in the recent times as it tracked gold in turbulent times on account

Exhibit 21: Silver & LME Index



Source: Bloomberg & KCTL Research

of safe haven properties. The year 2010 till date has seen the correlation between silver and LME Index, base metals' index on London Metal Exchange, weakened drastically. During the last three years ended on Sep 24, 2010, the correlation between them was found to be 0.7 which is pretty considerable. The Exhibit 21 shows both silver and base metals moving in same direction, except in 2010 when the relationship weakened. The volatility across the time periods also varied.

The above mentioned relationship fits relatively better if compared to copper, specifically. On three year basis, the correlation between silver and copper turns out to be 0.74 against merely 0.27 in the current year 2010 till date. On five year horizon, the correlation between the two was recorded at 0.55. Currently, the ratio trades at 94.68 levels which means it would take 94.68 ounces of copper to equal the value of 1 ounce of silver. During Q3 2010, the average ratio was 91.84 against 93.10 in the penultimate quarter on Comex. This year's average was recorded at 89.54 levels. The ratio may move higher because of silver expected to outperform copper.

Exhibit 22: Silver/Copper Ratio



Source: Bloomberg & KCTL Research

CFTC reports also point to silver's upside as shown by nearly 18% build up in net long positions of non-commercial holders, also known as speculators. Their long positions rose more than 30% to 62013 contracts as on Sep 21 from 47455 contracts on June 29, 2010. Short positions have more doubled to 12642 contracts from 5545 contracts during the same period. Commercial holders were net sellers of the white metal with net short positions of 65303 contracts as on Sep 21 against 58509 contracts on June 29, 2010. Total open positions have advanced about 15% for the aforementioned period.

The long awaited break in silver prices gave an extremely positive sign to silver bulls. It gave a clear signal that the price of silver was set to go higher. What we have seen in the last few weeks has been more than what we anticipated in our previous quarter's projections. Since prices have blown through \$20 and then \$21, it may now see some consolidation in the short term. There seems to be some steam left in this current move before we see a pull-back. Silver may seem to be in overbought territory at current levels, the action in the last few weeks is a strong signal to add silver as a pivotal asset to overall portfolio. Even if the prices correct in the short-term, its going to be short lived. Silver is still grossly undervalued and trading less than 50% of its previous all time high of around \$50/oz in 1980. And, we believe that the momentum in silver is just getting started and thereby, prices are headed much higher over the next 3-5 years.

Technical Analysis

Silver traded higher throughout the quarter and extended its winning streak to the seventh straight quarter.

Momentum indicator study: The momentum indicator RSI quarterly is trading at 0.721 levels, suggesting prices to be on bullish note for the coming quarter. Silver is witnessing a RSI positive divergence. Another momentum indicator Stochastic indicates prices to move higher as K% and D% are trading at 0.989 and 0.737, respectively. There is no sign of turning down or over lapping of K% and D%.

Pattern study: Silver made a break out on the upper side at \$18.60 levels which was a neck line for the *“Inverted Head & Shoulder”* pattern. The pattern suggests the target of silver is the length of the Right shoulder i.e. \$23.30.

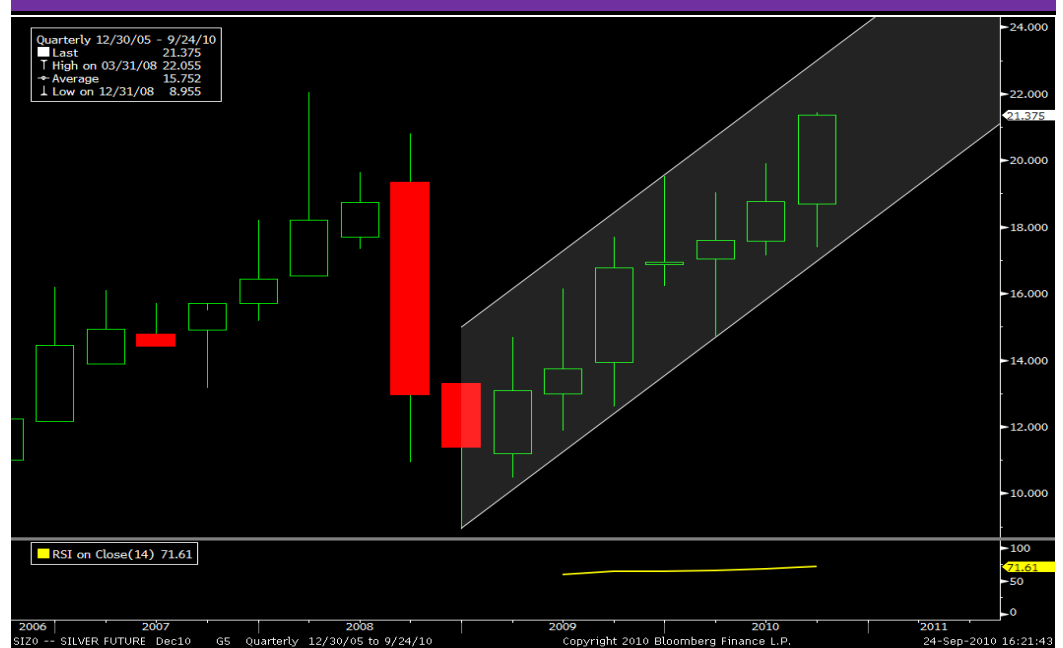
Trend line study: Silver is witnessing a *“Trend Channel”* pattern on the upper side on monthly chart which is also an indication for the prices to trade higher.

Quarterly Pivot Analysis

Exhibit 23: Pivot Table

Exchange	Support 2	Support 1	Pivot	Resistance 1	Resistance 2
COMEX	15.75	18.60	20.42	23.44	25.09
MCX	28154	29704	31516	34878	36690

Exhibit 24: Silver Technical Chart



Source: Bloomberg & KCTL Research

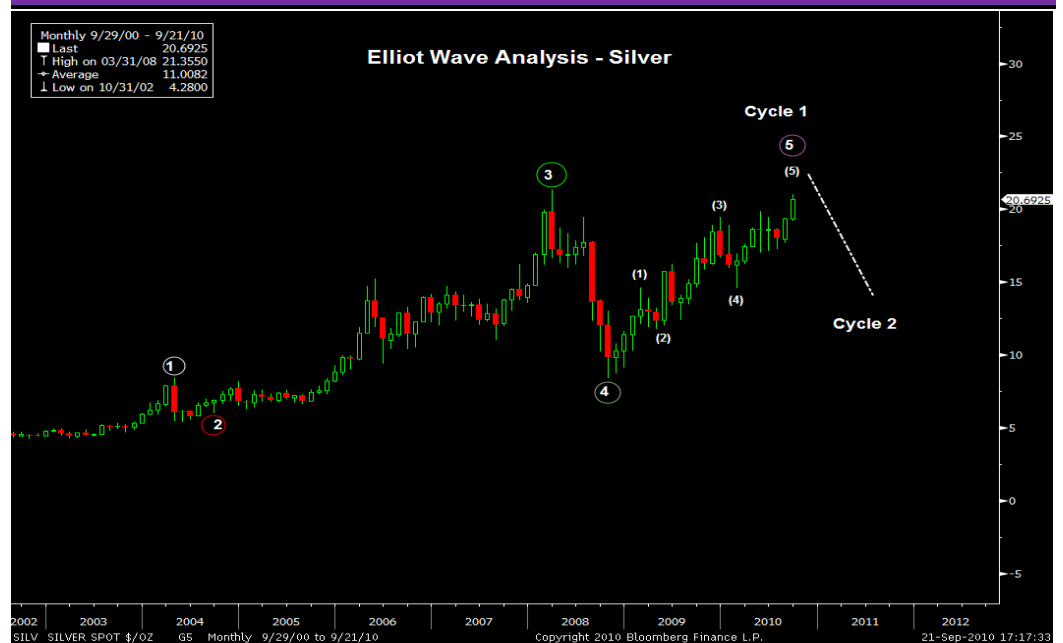
Elliot Wave Analysis

View: Upside

Strategy: Buy

Recent wave: Minor Wave 3 of intermediate wave (5) is in progress, which is likely to extend its gains till \$23.1 or till \$24.29 levels followed by a corrective wave 4 leads the prices to see downside correction till 21.8 or it can extend up to \$21.3 levels. Thereafter, a minor wave 5 is unfolded with upside bias till 25 levels or even more. On the downside strong support is seen at \$19.82 levels. Sustained trade above would lead the prices to remain higher.

Exhibit 25: Elliot Wave Chart



Source: Bloomberg & KCTL Research

Exhibit 26: Recommendations

COMEX (\$/oz)	Buy at 20.50 – 20.70 TP 22.50 then 23.50 SL 19.00
MCX (₹/kg)	Buy at 31600 - 31800 TP 34600 SL 29100

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