Pitchfork Playground Weekly Newsletter

45th Edition, 17 August 2014

GDX has been in a confirmed downtrend since September 2011 with price making lower highs and lower lows. This trend appears to be changing. Starting from the low in late-2013 we have one swing high and one higher low. Higher lows and higher highs is the definition of an uptrend.

As further confirmation of a nascent uptrend we have the 10 week moving average crossing above the 40 week average. 10 weeks and 40 weeks are equivalent to the 50 and 200 day averages in a daily chart.

Price popped above the lower median line of the regular-Schiff pitchfork in late-June and has been in a sideways consolidation since. Tim Morge refers to these sideways ranges as energy coils because price is storing energy for another move. Given that we are moving into the strong season for the precious metals and we already have an uptrend started, the next move is likely to be upwards.

GDX - Gold Miners ETF - weekly

Let's use this daily chart of GDX to examine volume action. In mid-March GDX rose to $28.03 and then started to decline. Volume receded along with price which is just what we would expect during an uptrend. In late-May selling volume spiked as price dropped below a horizontal support level - this was a capitulation selloff as weak hands puked their shares into the market.

Capitulation selling is often seen at the end of downtrends but we are assuming that the downtrend in GDX ended back in December. Can we explain this discrepancy in time? One possibility is that the 50 / 200 crossover in late-March attracted new money into GDX and the subsequent failure of this crossover in mid-May caused these marginal holders to exit. Some long-term holders may have also given up at this point assuming that the failed crossover marked the start of another significant downtrend. Regardless of the cause, capitulation selling is a good thing - it takes the weak hands out of the picture and strengthens the overall market.

After the capitulation GDX started another upward move that took price through both the 200 and 50 day moving averages. Volume increased with price during this move. Then GDX ran into resistance at the lower median line of the regular-Schiff pitchfork before gapping higher. Gaps are a sign of high energy and this was an upward gap on rising volume.

For the last two months price has been consolidating in a mostly sideways pattern. This is a lengthy period of basing which gives GDX plenty of time to consolidate the previous upward movement and to store energy for the next move. The fact that volume has declined during this consolidation is another indication that we are witnessing a new upward trend. In an uptrend we want to see volume rise as price rises and then decline as price pulls back or consolidates.

GDX - Gold Miners ETF - daily

The HUI looks essentially identical to GDX so we won't spend any time analyzing this chart.

Notice however that the 10 week average is rising steadily and price is finding support at that level - look at the last two price bars relative to this moving average.

HUI - Gold Bugs Index - weekly

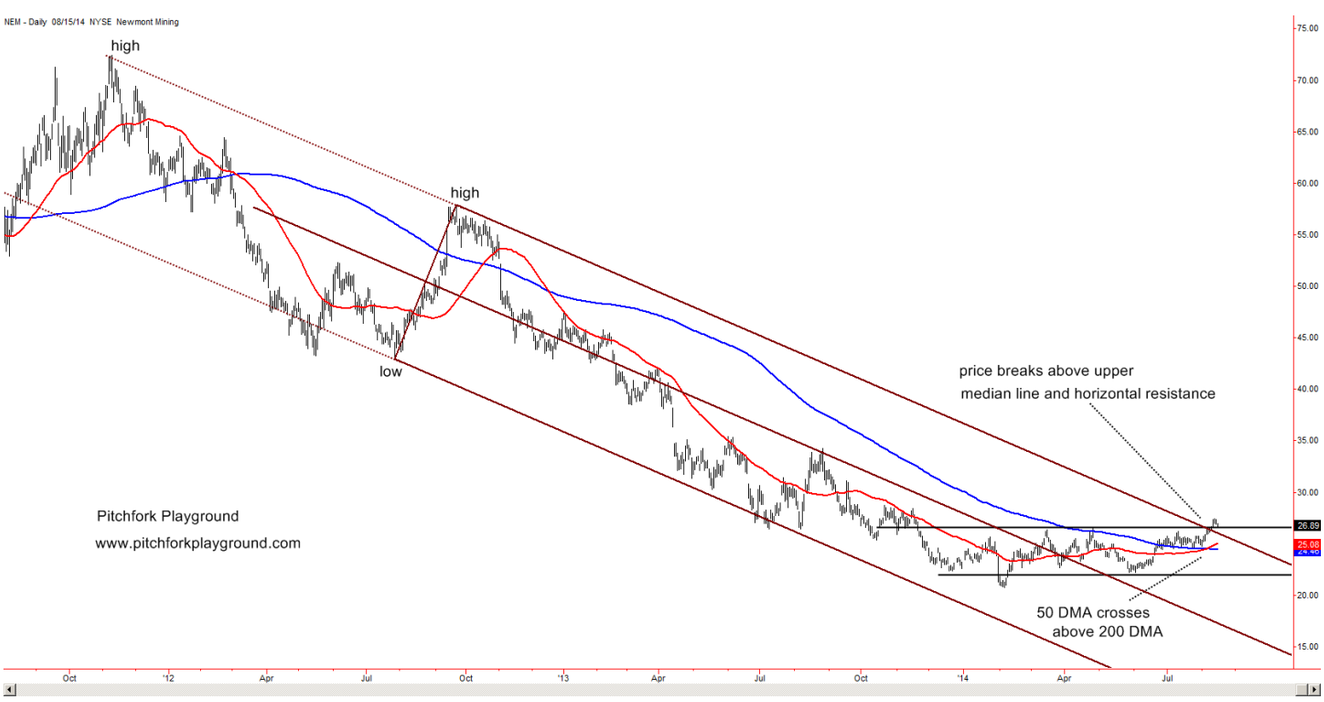
Goldcorp looks very similar to GDX and HUI in the weekly timeframe. A breakout above $30 and the upper median line of this modified-Schiff pitchfork would be another significant sign that the precious metals stocks are back in rally mode. Last week's price bar rose above the previous high at $29.27 so technically we have a higher low and a higher high in this nascent uptrend (although some might call it a double-top at this point).

GG - Goldcorp - weekly

While the other charts we have looked at so far are consolidating, Newmont has staged a breakout. We have the 50 day moving average crossing above the 200 day average price and coincident with this crossover price pushed through horizontal resistance and the upper median line of the modified-Schiff pitchfork. On Friday price pulled back for a test of the breakout level. In an uptrend resistance becomes support so we'd like to see NEM establish support at this point and then move higher.

NEM has been a leader in past precious metals rallies so we should expect it to at least participate in future rallies even if it doesn't lead. This breakout suggests that our expectation will be met.

NEM - Newmont Mining - daily



Royal Gold has already formed a higher swing high and two higher swing lows in its new uptrend. In late-June RGLD rose above the prior high from March so whenever we get another pivot high point we will have a second higher high in this budding upleg.

There are two modified-Schiff pitchforks in this chart. The larger one (dashed lines) did a good job of describing the price action up to late-May when the low point formed at the fork's median line. Since then the fork drawn with the solid lines has come into play and is doing a great job of showing us where to expect support and resistance. Notice how price is channeling higher between this fork's median line and the sliding parallel drawn with the dotted line. This channeling action is essentially an upward sloping energy coil or high base pattern. RGLD is consolidating but there is so much upward energy that price continues moving higher during the consolidation.

If we assume that precious metals stocks are moving into rally mode during their seasonal strong period, then we want to have positions in the strongest of those stocks. RGLD should probably be on the list of strong stocks.

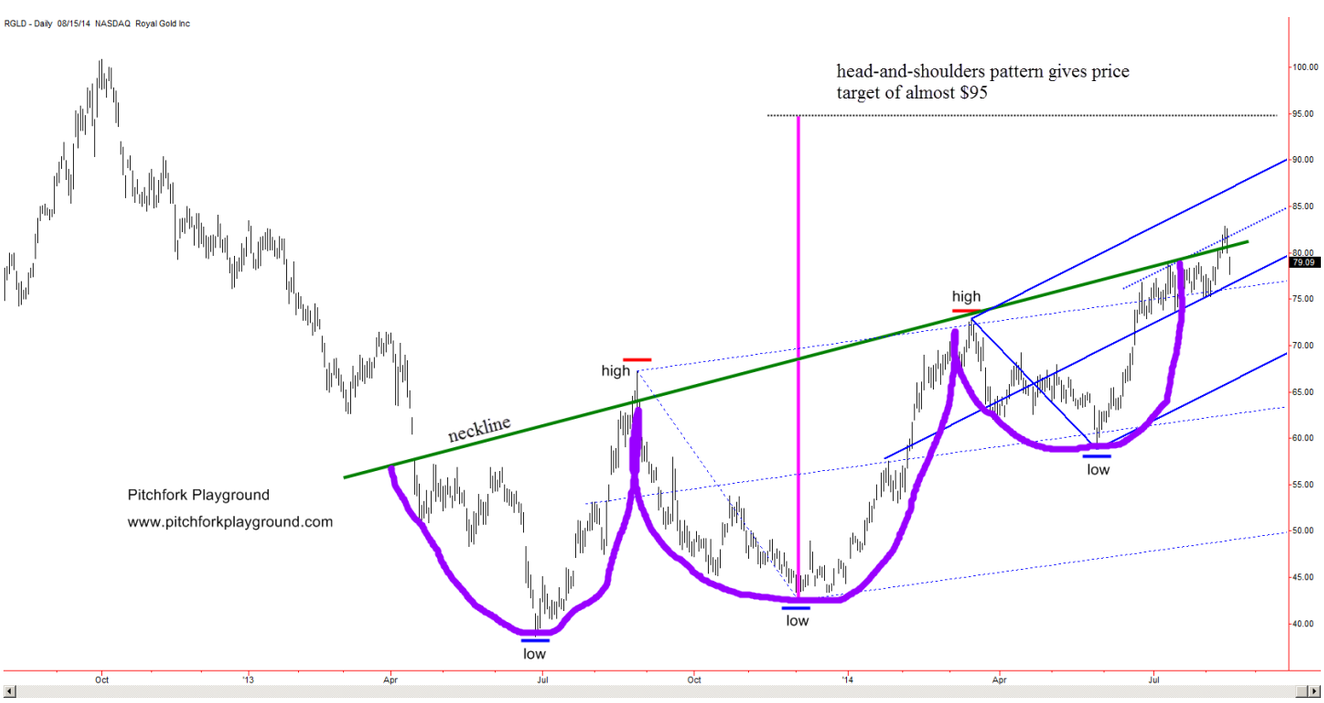
RGLD - Royal Gold - daily

While examining Royal Gold's chart I noticed this head-and-shoulders pattern. This isn't a pattern I typically look for because they seem to appear everywhere when you are looking for them. This one however seems worthy of notice since it took over a year to form.

Here's what Edwards and Magee ("Technical Analysis of Stock Trends") have to say about the head-and-shoulders pattern: "There are certain patterns which do allow the chartist the opportunity to project at least an interim target level of the direction of the Primary Trend. The most important of these patterns are found to be Triangles, Rectangles, Head-and-Shoulders, Pennants and Flags. ... The head-and-Shoulders Pattern has one of the better measuring sticks. In either a Top or Bottom, the interim target, once the neckline is penetrated, is the distance from the Top (or Bottom) of the head to the level of the neckline directly below (above) the head".

To find the target here we draw a line (pink) from the neckline down to the low point of the pattern's head. Making a copy of this line we place it above the neckline and see what price level corresponds to the top of the copied line.

RGLD - Royal Gold - Head-and-Shoulders - daily

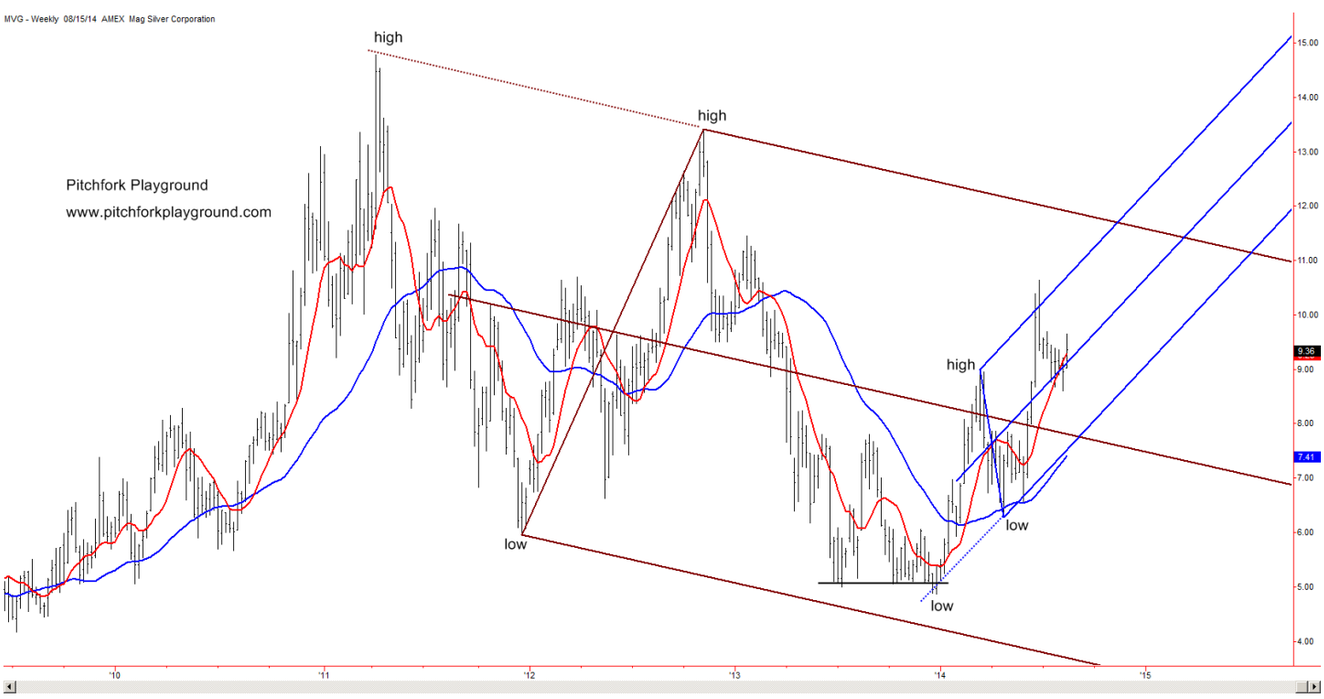


Silver Wheaton seems to be struggling with the median line of the blue modified-Schiff pitchfork. This level has been stopping price for several weeks. Last week we got a low energy bar (close in lower third of bar) after price was rejected at the median line once again.

SLW - Silver Wheaton - weekly

Mag Silver is looking good in this weekly chart. We have one higher low and one higher high and price is currently working to establish support on the median line of the modified-Schiff pitchfork and the 10 week moving average. Assuming that this support level holds we will have our second lower low.

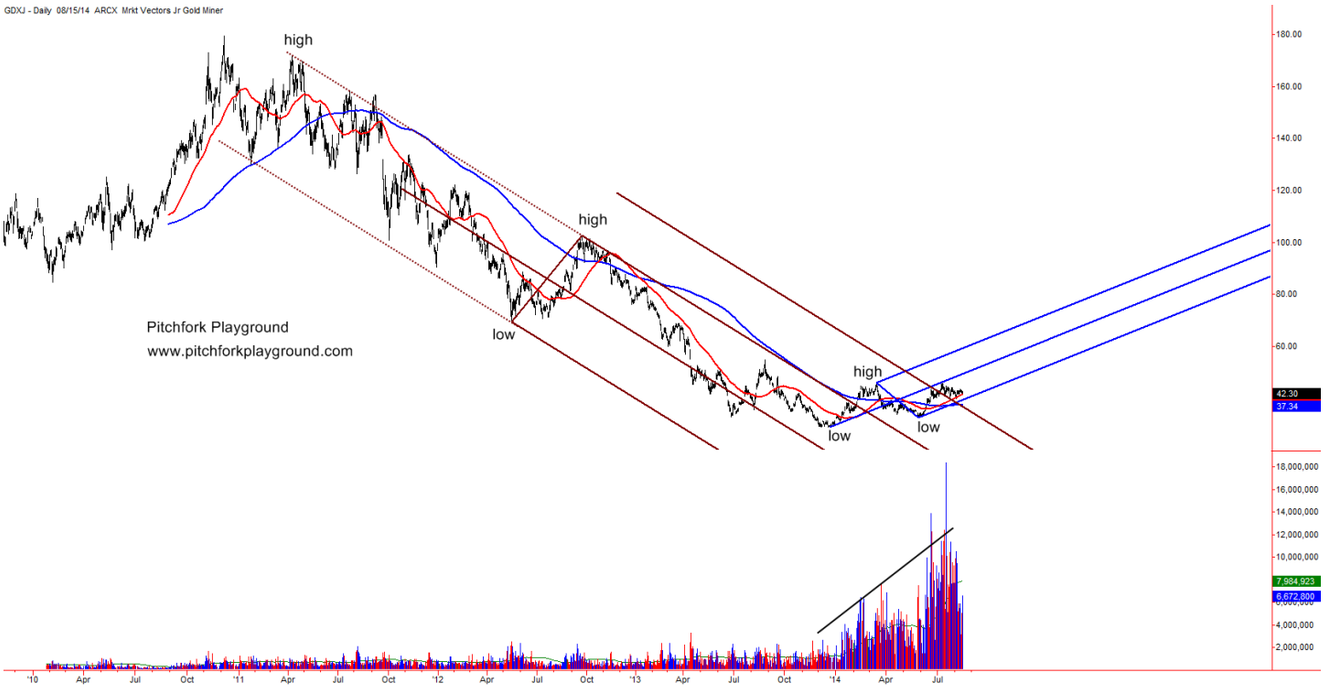
MVG - Mag Silver - weekly



If we were still looking for evidence of a new uptrend in the precious metals stocks we might finally be convinced by the volume action in GDXJ. Somebody is accumulating this ETF and it makes sense to assume that it is the so-called smart money doing the accumulating. When the precious metals stocks rally the junior stocks tend to outperform. Given this tendency it isn't surprising that institutional investors would accumulate and overweight the juniors before loading up on the more established mining stocks.

Let's take a look at who some of the institutional investors in GDXJ are. From the NASDAQ summary we find that (as of 6/30/2014) 37.5% of the outstanding shares are held by institutional investors. Morgan Stanley has 5 million shares, Deutsche Bank has 3.5 million, Citigroup has 2 million - that's 10 million shares held by the top three investors. Soros Fund comes in 6th with 760,000 shares and Sprott Inc. is number 13 with 332,000 shares. These are heavy-hitters in the investment world and they are choosing to invest in GDXJ. Perhaps they believe that the bear market in precious metals stocks is over or nearly over?

GDXJ - Junior Gold Miners ETF - daily



If we zoom-in on the daily action in GDXJ we see the same kind of volume pattern that we saw in GDX. Volume rises when price rises and then declines when price pulls back or moves sideways. We also find the capitulation selloff in late-May before price heads higher.

In early-July price broke above the upper median line extension of the red modified-Schiff pitchfork (see chart above). Not long after this breakout price ran into horizontal resistance from the prior high and retreated to the red median line. Finding support there allowed GDXJ to shift into a sideways consolidation move that is still ongoing. Notice how the recent action is finding support along the 50 day moving average.

We want to see price move above the horizontal resistance at $45.90 and then challenge the median line of the blue Andrews pitchfork. A break above those two levels would go a long way towards confirming the nascent bull market in mining stocks. Given the volume in GDXJ this breakout is likely to occur with a great deal of energy.

GDXJ - Junior Gold Miners ETF - daily

Alright, so we've looked at a handful of precious metals stocks - now what? Do we buy now? Wait for a breakout? And assuming that we want to put some of our hard-earned money at risk in this sector how do we go about it? Buy individual miners, the ETFs or a mix of both? What about long-term options? These are the tough questions that each of us must answer for ourselves.

On the one hand it is painful to miss a breakout and watch the vehicles we would like to buy move out of our buy zone. On the other hand it is painful to put money into the markets and have that money stagnate as the vehicles we bought go nowhere. Even more painful is putting money into the markets and losing some of it because we were wrong on direction. Each of us has to weigh these potentials as we decide how to trade.

To be conservative we can wait for more confirmation of the nascent bull rally before entering. Here are some factors that would further confirm that the mining stocks are going to rally into the Fall:

- GDX breaking above $28 and then $30
- HUI breaking above $260 and then $285
- GG breaking above $30 and then the upper median line of its weekly pitchfork
- NEM breaking above $28.50
- RGLD breaking above $85
- SLW breaking above $29
- MVG breaking above $10.65
- GDXJ breaking above $46 and then the median line of its daily pitchfork

The more of these breakouts that occur the higher our confidence will be in the nascent rally. And it won't kill us to wait for confirmation. There will always be pullbacks where we can enter and there are numerous mining stocks for us to play. If the miners are going to rally this Fall we should be able to scrape a nickel or two off the table without taking tremendous risks.

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That's all she wrote this week, folks. [This saying, "that's all she wrote", likely originates in the 'Dear John' letters of WWII. The American GI is reading a 'Dear John' letter to his buddies and finishes with, "That's all she wrote".]

Before we wrap up let's touch briefly on the equity markets. The Dow and S&P 500 have had healthy pull backs in recent weeks and have now rallied back up to resistance levels. Based on the charts we would have to say that these markets are experiencing bear rallies and we would expect another leg down to begin at any time. On the other hand we had lots of bad news last week which should have given the markets plenty of reason to head lower if they were going to. The fact that they ignored the bad news suggests that we are still in a primary bull market with the markets headed back to their previous highs. As another sign that higher prices lie ahead we have the NASDAQ chugging merrily along while the Dow and S&P 500 dropped. To confirm a resumption of the uptrends we'd want to see the S&P move up through 1960 and the Dow above 17,000.

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"Twenty years from now you will be more disappointed by the things that you didn't do than by the ones you did do ."
~ Mark Twain