

April 17, 2013 – Aftershocks

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Emails from subscribers were most interesting this week, following the historic fall in precious metals prices on Friday and Monday. One made a simple observation that really struck a nerve. The subscriber, from Switzerland, expressed surprise at the harsh general media commentary on the sudden and historic fall in prices, particularly in gold. There seemed to be a spontaneous outbreak of almost universal condemnation of gold, ranging from sermons on why gold will never go up to what amounted to I told you so's from folks I didn't think even followed the price of gold. It's no joke to say gold is the most emotional investment and I was well aware that some of its proponents can get over-enthused at times, but I was more taken aback with the outburst of hatred the price smash brought. It was as if multitudes of gold haters which were silently suffering through a decade of outsized price gains were suddenly redeemed and free to comment on how lousy was this commodity.

I guess that goes with the territory of being the most emotional commodity, but lost in the venom being poured on gold are some basic observations that are being overlooked. Whether you are a gold supporter or not, the two day price smash of more than \$200 was one for the record books. More than \$1 trillion was erased from the value of the world's gold market capitalization in the relative blink of an eye. Whenever 15% of the value of a major world asset class evaporates in a flash, it is appropriate to uncover the reason, lest that reason slip into other markets, like stocks and bonds. Strictly for self-interest purposes, any time a big market like gold falls 15% in two days, we all should be concerned whether that can happen elsewhere.

For instance, do you think a 15% two day drop in the Dow Jones Average, or more than 2200 points, would go unexamined on a forensic basis for what caused it? Of course not, and that was the reaction to past stock market crashes. As I've tried to explain, this big and selective commodity price smash had to do with the mechanical process of certain large traders (JPMorgan in silver) deliberately rigging prices lower to induce margin call panic selling. All the gold naysayers and I told you so's should stop their lectures for a moment and question how and why any market can fall so much so quickly, as that indicates something is amiss. Most importantly, it should be the regulators' first mission to uncover what happened on Monday and Friday, but that is unlikely to occur due to an inherent bias concerning certain markets, including gold, silver and oil, especially when those markets fall sharply. Sadly, one of the crosses precious metals investors have learned to bear is the CFTC looking the other way when anything results in a decline in metals prices. It's just the way it is and you're not crazy for feeling discriminated against.

For the record, I'm neither a gold hater nor gold lover. As a supply/demand commodity analyst, I much prefer silver compared to gold, but as an advocate of free markets, I am appalled at the lack of regulatory action against those clearly rigging our markets, gold included. I am also appalled at those commentators so relieved that gold finally fell in price that they won't question or acknowledge the suspicious trading irregularities behind the smash.

Let me preview this week's upcoming Commitment of Traders Report (COT) which will include Friday and Monday's historic price drops. Needless to say, this will be an extremely important report and I intend to examine it with an open mind and not with preconceived notions. I do expect a large amount of commercial net buying and technical fund and other speculative net selling, as that would be in keeping with my basic understanding of how the markets work. I'll be paying particular attention to the sub-category changes, like JPMorgan and raptor activity as well as the nuances in the managed money categories.

Whether the net commercial buying comes in close to my guess of 40,000 contracts or so in gold and 10,000 to 15,000 in silver (and copper) is less important than my sense that this was the mother of all liquidations and all we're likely to see going forward. In other words, this report should register the maximum amount of speculative selling possible, whatever the actual numbers, given the extreme volume and price carnage recorded. It's hard for me to imagine significant future net commercial buying because I can't imagine much speculative selling being left after Friday and Monday. But then again, I hadn't imagined much being left before the crash.

I've had a few questions from subscribers about the raptors, the smaller commercials apart from the largest 8 traders. The raptors went into the price smash with a record net long position in COMEX silver futures, around 31,000 contracts (but only 7000 contracts net long in COMEX gold). The sudden two day \$5 drop in silver resulted in a negative mark to market move of \$775 million for the silver raptors. This is the total negative money change (and prospective margin call) for a group that I would estimate at maybe 20 or so traders. Evenly divided, that comes to almost a \$40 million sudden hit per raptor.

This record and unprecedented negative turn of events may have caught a few (or more) raptors off-guard and they may have been forced to sell at a big loss (for the first time ever). One of the things I'll be looking for is to see evidence of this in the new report. I would not fall down shocked if JPMorgan intended to turn on the raptors (as well as other long speculators) as a source of forced selling so that JPM could buy much more. I always imagined JPMorgan taking away the raptors long position on sharply higher prices, but the sharply lower prices just witnessed may have been intended from the get go. Dinosaurs do eat other dinosaurs.

Likewise, it's possible that the technical funds which have been heavily short recently may have rung the cash register and bought back some shorted silver contracts at big profits, although I'm inclined to believe only a few may have done that. The important point is to be on the lookout for whatever data the report reveals without preset forethoughts on how to interpret it. However, given my prior experiences with extreme silver sell-offs, I must conclude there was nothing accidental about this one. I will be shocked if JPMorgan (the big 4) hasn't bought back big, regardless of the changes in other categories.

Although these are unusual times, we must still be vigilant and logical in sorting through the commentary and analyses explaining these times. For instance, there has been increasing talk that as a result of the big price takedown this heightens the chance of a COMEX delivery default in gold and silver. While the possibility of a COMEX delivery default has been raised by me for years as a consequence of an artificial low price, I can't see how that extends to gold at this time. I'm aware of the extremely tight silver and even gold retail situation, but, so far, it hasn't crossed the firebreak into wholesale.

But there is one special factor that will make it a surprise to me for there to be a delivery default dead ahead. There appears to have been a massive decrease in the total net commercial short position in COMEX silver and gold. As such, the short "hot potato" has been tossed by the commercials to the technical funds. It seems to me that contract default occurs when important short holders are left with no choice but to finagle their way out of delivering the actual merchandise. With a greatly reduced short position, the commercials have little reason to default now and if it is the technical funds heavily short, I wouldn't think they would be able to default; they would be made to cover and buy back, regardless of the price. Who do you think runs the exchange? JPMorgan or some stinking tech funds?

Most often, previous extreme silver sell-offs (and there have been too many) occurred after strong price run ups. This one is different in that it occurred at what had been a low price point and relatively low levels of the total net commercial short position. Also different is that silver was only one of the selective NYMEX/COMEX markets that took a pounding this go-around. That makes this silver sell-off much more unusual. Invariably, all past extreme silver sell-offs have proven to be the best buy point possible, as I'm sure this one will prove to be. Still, the different aspects to this sell-off strongly suggest this could be the set up for the big move up.

There seems to be a mirror-image quality to the current set up to what we have seen at previous silver market tops. At previous tops, the technical funds were long and had massive open trading profits while the commercials held equal and commensurate open trading losses. At those tops, the question was always would the commercial shorts get over run for the first time? Somehow, the commercials always prevailed in the end and the price came crashing down in time. This time, the technical funds which are short are also holding massive open profitable short positions and one group of commercials, the raptors, are long with open massive losses. JPMorgan, of course, has been in the catbird seat by being able to buy back short positions at massive realized profit.

At previous tops, at least there was a chance the commercials could get over run for the first time ever. In this current set up, the chance that JPMorgan and most of the raptors could be over run to the downside by technical fund shorts seems as remote as the farthest star in the universe. But make no mistake. This is essentially the bet a silver investor is making at this point, namely, that JPMorgan and other commercials will prevail against the technical fund shorts. Of course, all the same great silver supply/demand fundamentals still favor silver rising sharply in price, but perhaps the most bullish factor ever has just appeared on the scene. For the first time to this extreme, the crooks in silver, led by JPMorgan, are better positioned for an upside move than ever before.

Markets evolve constantly; there never is an end or last day. We, as humans, have an end day, but not markets. The recent price smash is not the end of the silver market, but rather a significant development towards the next price cycle. The combination of spectacularly bullish fundamentals, a sudden new low price and now the dramatic positioning by the important entities on the COMEX point to silver being a better investment opportunity than ever before. As much as it doesn't seem fair or that it was accomplished legally, the commercials seem to be better positioned than ever for a silver price lift-off. When and how remain to be seen, but these commercials do go for the jugular.

Ted Butler

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Silver – \$23.15

Gold – \$1375

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