

August 24, 2011 - The Root of All Evil

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Even for someone who has been consistent about the price volatility to come, the actual volatility being experienced is unnerving. I can only imagine how it must seem to those unprepared. My sense is that the conditions that led us to this point are still suggestive of volatility to come in gold and, especially, in silver. Just what were the conditions that brought us to this point?

Simply put, we are witnessing extreme price volatility in gold and silver due to excessive speculation in paper derivatives contracts. The volatility is not the result of sudden and legitimate changes in the supply and demand of actual metal. In a moment, I'll describe this excessive speculation in more detail. Two entities are responsible for this excessive speculation and the increased volatility it fosters. First is the CME Group which has done everything in its power to create more mindless and uneconomic trading because it gets compensated for the increased trading. Because the CME Group is willing to harm the public's general interest in order to achieve increased revenues, I refer to them as a criminal enterprise. In this regard, I consider the CME as similar to how the Mafia operates, namely, for its own financial interest with little concern for the public welfare. I honestly don't know who would be more offended with this comparison, the CME or the Mafia.

The second entity responsible for the excessive speculation is the federal regulator of derivatives trading, the Commodity Futures Trading Commission. Perversely, one of the prime responsibilities of the CFTC is to prevent excessive speculation from unduly influencing the price of commodities. How has it come to the point where the federal agency created to prevent excessive speculation has morphed instead into being a major cause of it? I think the answer lies in timidity, brought about by industry lobbying and influence. The CFTC is afraid to do the right thing due to industry pressure.

The holy grail for the derivatives industry is trading growth above all else. The industry profits from increased trading volume. Volume is increased when price volatility expands. Therefore, it is of little surprise for the CME to enact measures designed to increase volatility and trading volume. The problem is that increasing trading volume by encouraging greater volatility is not why the US commodity markets are allowed to exist. Commodity futures markets are allowed to exist to encourage legitimate hedging, not mindless paper speculative trading. Legitimate hedging involves real producers and consumers transferring price risk to speculators, not mindless day trading exclusively between speculators. My point is that the CME is more interested in increased HFT and other manipulative paper day trading and not in encouraging more legitimate hedging by real producers and consumers.

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If the CME Group is at the root of all evil as far as encouraging disruptive trading practices and increased price volatility, why is the CFTC sanctioning this scam? My best guess is that the agency is incapable and afraid to do the right thing. There is a natural degree of "regulatory capture" which is defined as occurring when a regulatory agency created to serve the public interest instead advances the interests of the industry it regulates. This fully describes the CFTC's role in dealing with derivatives trading and, in particular, the CME Group, the largest derivatives exchange in the world. The CME has captured the CFTC to an extraordinary degree. Compounding the problem is that the CFTC has denied the public's requests to end the silver manipulation for so long, that it is now in the additional position of being negligent for not acting sooner. I don't know how the officials at the CFTC can look at themselves in the mirror for their failure to serve the public with what is transpiring in silver and gold.

Since the weekly review a few days ago, the price volatility in gold and silver has been extraordinary. Gold first climbed by \$60 and then plunged by \$160. Over the same three days, silver first climbed by \$1 and then crashed by more than \$5. I have tried to explain why we climbed by more than \$400 in gold from July 5 and why we might fall (or further explode). That explanation involved the massive bet on the short side by the COMEX commercial interests that went bad to the tune of almost \$10 billion at the recent peak. Many are quick to claim that it was speculative buying that drove gold higher, but they are only partially correct. Technical funds and other speculators did buy and establish long

positions on the way up, but such buying mostly ceased at about the \$1600 level. The speculative buying that drove prices the last \$300 higher, from \$1600 to over \$1900, was largely panic short covering by certain commercials. I postulated that the market would further explode if and as more short covering occurred and that if that commercial short covering was satiated, prices could crash. It looks like we got both.

The bigger point here is that the true excessive speculation in gold and silver is by the commercials pretending to be hedgers. Yes, the technical funds and other long speculators certainly could influence prices and if the CFTC determined that to be the case, then the solution is simple – adjust position limits accordingly. But the same remedy applies even more to the true speculators – the commercials. These commercials take such large and concentrated positions so as to create the danger of the disorderly prices that we are currently observing in real time. These are the traders that the CFTC needs to crack down on via legitimate speculative position limits. These are the traders that deliberately disrupt our markets. These are the traders that have captured the regulators.

What next for gold and silver prices? Because the commercials were so badly hooked on the upside in gold, that increased their desperation to rig prices lower in order to recover their open losses. This made them more dangerous, much like cornered rats. Now that they have succeeded in creating a large sell-

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off, they will press prices lower until they can liquidate as many of their gold short positions as possible. I wish I could pinpoint that for you in time or price in advance, but I cannot. Based upon the extent of the price decline so far and the heavy volume accompanying it, the liquidation may be completed relatively quickly. I can tell you that the commercials were never in such financial distress as they were this time in gold and that they will be unlikely to sell gold short again as aggressively in the future. That augers well for the next gold rally.

Silver is in a somewhat different condition. The commercial silver short position, while always more concentrated and manipulative than the short position in gold, didn't grow as negative as gold's COT structure had become recently. Even though silver has now been manipulated sharply lower in price, that's due mostly to the corrupt nature of the silver market and the ease with which the COMEX commercial crooks can take it down, especially since the regulatory guard dog is sleeping and toothless. Therefore, it shouldn't be long until silver is washed out, as the high volume also supports. While I can't pinpoint when that will be, I am convinced that the rally following this deliberate wash-out is likely to be powerful, perhaps the most powerful rally ever in silver. Much of my conviction is based upon signals from the physical market and the coming resolution of the matter of position limits within the next month or two.

These sharp sell-offs are no fun, particularly when you come to understand just how deliberate they are. Even anticipating the likelihood of a sell-off doesn't

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erase the outrage at the criminal behavior of the CME commercial thugs and the complicit CFTC when it occurs. Once again, I can tell you unequivocally that the commercials were collusively buying every gold and silver contract they could over the past two days. It is not possible for the commercials to buy on such a consistent and unified basis to the downside without collusion present.

The only sure way to beat the silver manipulators at their own game is not to get shaken out of core holdings on the deliberate takedowns. Better yet is to add to positions when the commercials are buying, which is always on sharp sell-offs. Silver is always beaten down the most because it is the commercial crooks' biggest problem and they use any pretense to induce long liquidation. And if you feel the need to vent your outrage at this ongoing crime in progress, you should do that as well by communicating your feelings directly to the commissioners at the CFTC. What these people do all day is beyond me. You can find their email addresses in the August 10 article- The Public Be Damned.

Ted Butler

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Silver - \$39.40

Gold - \$1757