

Jan. 20, 2010 – No Fun

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Admittedly, that's overstating the obvious. There's a pretty severe smack down taking place in silver and gold today. I'd like to explore why it happened and what it means for the market. Please understand that I did not expect today's sell-off. But neither does that mean there are no logical explanations.

One of the advantages of having an Internet-delivered service is that you can disseminate information quickly, when readers want it the most, like on days like today. One of the disadvantages is that if you do disseminate information quickly, you can be proven wrong just as quickly. With that in mind, let me try to make some sense of what's occurred today.

There is nothing accidental about this move down in silver and gold. Yes, I know it didn't occur in a vacuum, and that there were plenty of other markets that have made extreme price moves today. I think this provided the cover story, or excuse that the big short sellers were looking for in order to harvest the technical fund longs on the COMEX. I don't complain that every day to day movement in the price of silver is as a result of the ongoing manipulation, as that would tend to undermine one's credibility. But, on the other hand, either a market is manipulated or it is not. Silver is a manipulated market. Today's action is clear proof of that.

The reason for that lies in the nature of the silver price moves, whether up or down. The ups are usually measured and orderly, the downs can be outright nasty, like today. There is a real simple reason for that. Because there is such a concentration on the short side among a very few big traders, there is no competition. This is why we have laws against monopolies, to prevent non-competitive market behavior. On the way up in price these big shorts must sell more to protect their existing large short positions and contain the price rise. When they can engineer a price decline (with the help of outside influences), these same big shorts band together, since there are so few of them anyway, and withhold their bids to buy back what the technical funds are selling. This is also called collusion. Only after the technical fund liquidation has exhausted itself, and the big concentrated shorts have bought back as many of their short contracts as possible, is the sell-off complete.

This is the force behind the silver and gold move today, nothing else. Certainly, there were not any developments in the real world of actual silver supply and demand that accounted for today's COMEX-dictated move that could account for the extreme price drop. Because this was a paper contract engineering that determined what the price of real silver will be bought and sold at for today throughout the world, the price of silver was controlled by the actions of the big concentrated shorts on the COMEX. There can be no clearer example of manipulation, as commodity law precludes paper contracts from setting the price of a commodity in the real world. Yet, that is exactly what we are witnessing today. The solution? Crack down on the big concentrated shorts, through position limits and disallowing phony hedge exemptions to those limits.

While today's one-dollar drop in silver is painful for holders of silver (not for new purchases, of course) and an affront to believers in the free market and the rule of law, it is important to put things in perspective. While down a dollar from yesterday's close, we are still up a dollar from the year-end close. And because the price of silver and gold is so much higher than it was years ago, we have to resign ourselves to the new level of volatility. A one dollar move today is equal to a 25 cent move when silver was \$4 or \$5. Rest assured, today's price volatility will look small compared to the size of the price moves down the road.

I know it isn't fair that the manipulators, primarily JPMorgan, can operate so brazenly and that the CFTC can sit by while this occurs, but we have to deal with it. Besides, there are some good things to be said about today's crooked sell-off. The volume has been heavy and there appears to be much liquidation of technical fund long/crooked dealer short positions on the COMEX. This won't be evident in Friday's upcoming COT, as the cut-off for the report was at yesterday's close. But the important thing is that the liquidation takes place, not when it is reported.

No can tell how far a short term move will carry, especially when the tech funds are on the run. But we can try to measure the extent of liquidation and make reasonable guesses as to when it may be complete. Barring some type of extreme and unexpected (by me) watershed liquidation, like we saw in 2008, today's liquidation appears to have brought us back to the levels in the COT at the end of December, when I advised deploying whatever dry powder that may exist. Fortunately, prices are still substantially higher than they were then, in spite of today's sell-off. As such, this price decline may not last much longer. I can't redeploy my dry powder, as it is already invested. But neither would I remove it. Those that do have investable silver funds should buy here and on a scale down basis.

Thanks to all who wrote in to commend the CFTC for the milestone meeting. To be frank, I don't feel like commending them much today, but we must stay on a course to the end. What is the end? Two incredibly specific things. One, the position limits in silver must be made to be roughly one-quarter the level of opposition limits in gold. This is because the open interest in gold is four times that of silver, and the CFTC's and CME Group's formula revolves around total open interest. I don't even care if gold position limits are kicked up dramatically higher and silver is left unchanged. That will still prove silver's and gold's limits were wrong all along, proving the exchange had it wrong for decades and has no right to determine anything regarding position limits.

Two, by the end of this process, the CFTC and CME Group will have to explain why big shorts, like JPMorgan, are allowed to hold such big concentrated positions, in spite of the obvious manipulative impact of those positions. If the CFTC, under Gary Gensler, manages to avoid such an explanation at the end of the proposed hearing on precious metals that will be a clear signal to me that the Commission will never address this issue openly and honestly. Here's to hoping that doesn't happen.

PS. I keep forgetting to mention that I will be speaking at the Cambridge House Investment Conference in Phoenix on February 4 and 5. I'm not much of a traveler, but I did attend this conference last year and will be there this year as well. Please come by if you can

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