May 2, 2011 – Night Moves

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In a shameful display of a Self Regulatory Organization (SRO) failing to regulate, the CME Group allowed the big commercial insiders on the COMEX to engineer a price smash when silver trading conditions were at the lowest liquidity possible. I have previously referred to the CME Group as a criminal enterprise. I didn't go far enough.

In a 12 minute time window early Sunday evening, silver prices plunged as much as $6 in COMEX (GLOBEX) electronic trading, on exceedingly low volume. That's more than a 13% drop in minutes. I'm not aware of any other silver market open at that time, especially as markets in London and Asia were closed for the day. In a very literal sense, this was all a COMEX affair. As such, this proves the exchange is at the heart of the silver manipulation. The intent behind this contrived sell-off seems simple to me Â? it was designed to flush out any resting stop-loss orders placed below the market. And that it did.

Basically, it appears to me that the commercials are pulling out every dirty trick in their manipulative bag of tricks to shake every leveraged long speculator possible from the market. First, as indicated in the COTs, they aggressively bought back on new high prices over the past few weeks. Now they have given the silver apple tree another good shake to the downside to rid any speculative long hangers on. As a result, there remains very little leveraged long silver fruit to shake off. This shakeout greatly improves a market structure that was great to begin with. It may not feel so at the time, but these flush outs are constructive towards higher silver prices.

For those wondering how it is possible to knock a market down so much as occurred last night, I believe it has to do with the crazy high frequency computerized trading (HFT) that has come to infect the silver market (it's not particularly obvious in gold). This is the same mindless computerized trading responsible for the infamous flash crash of a year ago in the stock market. This type of trading greatly increases trading volume (which the CME worships), yet does nothing to enhance true liquidity. HFT is uneconomic and benefits no one except the exchange and its few practitioners who use it to set prices. Commissioner Bart Chilton has taken to call these traders Â?cheetahsÂ? due to the speed of their trading in and out. A more appropriate term is cheaters.

The clear fact is that there was no price discovery last night in the smack down of silver. There was no news or no supply/demand developments to account for the silver price movement. There was no physical trade in silver, only electronic games. This was purely illegal price setting on a crooked exchange by a handful of manipulative commercials. It was a direct slap in the face to CFTC. But it would be a mistake to let the COMEX crooks intimidate silver investors and scare them out of silver holdings. The best way to do that is not to hold margined COMEX positions. Hold fully-paid for positions. If you need leverage, stick to options and preferably in SLV and not on the COMEX. The important take away here is that the commercials are buying any way possible. I think they are doing so because the physical silver shortage is about to hit with full force.

I'd like to follow up on the matter of the excessive short position in the shares of the big silver ETF, SLV. Due to space limitations, I may not have properly conveyed just how important an issue this is. I would rank it as serious a matter as the original COMEX silver manipulation, which I first identified more than 25 years ago. To illustrate just how large and uneconomic the current short position is in SLV, please allow me to make some comparisons.

Let's first compare the short position in SLV to its most logical counterpart, the short position in the big gold ETF, GLD. The current short position in SLV is 36.7 million shares. Since the total number of shares outstanding in SLV is 363 million, this means the short position is a bit over 10% of all shares outstanding. This is a very high percentage, as most stocks have a short position that generally amounts to less than 1 or 2 percent. The GLD also runs higher than the average and has a short position of 22.4 million shares against a total of 405 million shares outstanding and a short percentage of about 5.5% of outstanding shares. So in this case SLV has almost double the percent short as does GLD. But since these are hard metal ETFs, some further comparisons are helpful. http://www.shortsqueeze.com/?symbol=slv&submit=Short+Quote%99 (type in GLD for data)

The SLV short position is equal to 36.7 million ounces of silver, while the GLD short position is equal to 2.2 million ounces of gold (one-tenth an ounce for each share of GLD). Compared to the annual production of each metal (740 million for silver and 80 million for gold), the SLV short position is again almost double the size of GLD in percentage terms (4.9% in SLV versus 2.8% in GLD). However in terms of all the silver and gold bullion in the world (one billion silver oz vs. 3 billion gold oz) the SLV short position is 50 times the size of the GLD short position in percentage terms.

My favorite comparison of the relative short positions in SLV and GLD is in terms of the net amount of silver and gold available for investment. If you recall, this was a concept I introduced in Â?Silver Investment Supply/DemandÂ? (in the archives March 30, 2011). I estimated in that article that there were approximately 10 to 12 million ounces of silver available for investment demand each month (after industrial and other fabrication). In gold, there were about 4 million ounces available each month for investment. So in terms of investment demand, the short position in SLV represents a full three months of demand. In gold, the short position in GLD is about two weeks worth of investment demand.

Aside from the comparisons with the GLD, I would ask you to think about the short position in SLV versus what silver is available for investment in another way. I think this is the key. Since SLV is clearly a proxy for physical (as is spelled out in the prospectus) any short sale short circuits or frustrates the investment demand for silver by substituting the short paper sales for real silver that should be deposited into the Trust. In other words, had the short sellers been disallowed from making an end-run around the prospectus and were forced to deposit silver in the amount of more than 36 million ounces, the price would have been much higher. How much higher? My guess is the price of silver would now be $60 to $75 were it not for the fraudulent short sales in SLV. That's at the heart of this fraud and manipulation. That's the reason the short sellers sold short in SLV, they couldn't get the silver and they didn't want the price to reflect the true supply and demand.

Because of the fraud and manipulation in the short selling of SLV shares and its impact on the price of silver, this practice has emerged as a most serious issue. The only question remaining is who is behind it? Even though BlackRock is the owner and sponsor of the SLV, I don't think they are the bad guys. In fact, my guess is that they weren't even aware of this issue until I wrote to them last week.

I'm a firm believer in assuming innocence until guilt is proven. BlackRock has an impeccable reputation and no clear motive to actively participate in this short selling scam. But it will be how they handle this situation that will determine if they maintain their good reputation. Make no mistake, BlackRock, regardless of what they may say or not say publicly, will be judged on the future course of the short position in SLV. If the short position doesn't decline significantly and soon, that will reflect badly on BlackRock.

In the meantime, don't be frightened by the SLV short position, as it will be resolved. The best example I can give you is to compare it to the excessive short position in COMEX futures. For many years I lambasted the COMEX short position but simultaneously pointed out what a powerfully bullish force it provided in silver. Same thing with the SLV short position Â? it's fraudulent and manipulative, but it will prove highly beneficial to the price. The big difference between the COMEX short and the SLV short is what is done about it. The COMEX management and JPMorgan tried to ignore the problem hoping it would go away. Guess what Â? they were wrong. Let's see if BlackRock steps up to the plate and does the right thing.

Ted Butler

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Silver – $45.80

Gold – $1559

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