May 20, 2010 – The Other Flash Crash

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Most market observers are now aware of the infamous 1000 point Â?Flash CrashÂ? in the Dow Jones Industrial Average on the afternoon of May 6. It rattled the nerves of investors worldwide. Intense scrutiny at the highest levels has failed to uncover the specific cause behind the crash. Increasingly, the likely culprit appears to be a sudden withdrawal of liquidity by high volume traders. With no reassurance that this event can't be repeated, anxiety runs high. About the only good thing to be said about the May 6 event is that no suggestion has been made that it was intentional. Still, all efforts must be made to prevent its reoccurrence.

Today I would like to discuss another flash crash; the one that has enveloped certain commodities, including silver, over the past few days. Upfront, let me point out the big difference between the stock market event and the flash crash in silver (and other commodities). The difference is that the silver and commodity flash crashes were planned and deliberate. Most of what I will say pertains to all commodities (mostly metals and maybe oil), but for the purpose of this piece I will reference only silver. That's where the market circumstances are always extreme.

The stock market crash appears accidental with no clear set of winners emerging from the debacle. The silver crash clearly rewarded the most dominant participants in the silver market Â? the large concentrated commercial short holders on COMEX, led by the largest short, JPMorgan.

Stock market trading has come to be dominated by extremely high volume institutional trading, run by super high-speed computers. The sudden withdrawal from trading by these high frequency traders (HFT) on the afternoon of May 6 caused havoc. The withdrawal of the usual buying and selling by these HFTs caused a void of bids as increased selling came into the market. The result was an instant void of bids which caused stock prices to suddenly plummet. There is no suggestion that the sudden absence of HFT liquidity was part of an intentional conspiracy to make stock prices crash. This appears to be purely in the unintended consequence category. Certainly, if any evidence does emerge that there was an intentional profit motive on someone's part to cause stock prices to crash, no effort should be spared to bring those responsible to justice.

Now contrast the stock market's May 6 event to what has just happened in silver. Like in the stock market, COMEX silver trading has also largely gone electronic, with pit trading now accounting for only two percent or so of total computer volume. Any sudden withdrawal of electronic bids in COMEX silver (or other markets) would have the same impact on price that occurred in the stock market on the afternoon of May 6. Take away the bids in any market suddenly, and you will have a sudden crash in prices. This is exactly what happened in silver and other commodities over the past few days. The bids were suddenly removed.

The difference in silver is that the removal of bids was intentionally designed by, and for the benefit of, the large COMEX concentrated shorts. These commercial traders, of which JPMorgan is the largest, collusively pulled their bids to cause prices to drop sharply, at which point they reinstated their bids to benefit from buying at the sharply lower prices. This can be proved in a number of ways.

First, there can be no doubt that the big commercials are the largest trading entities on the COMEX, by virtue of government-provided concentration data. In this sense, the commercial shorts are very similar to the High Frequency Traders who dominate trading volume in the stock market. If any one group of traders were the most capable of suddenly withdrawing bids in COMEX silver, it would have to be the concentrated commercial shorts.

Trading records will show that the commercials were big net buyers on the days of the largest price drops. That's an easy statement for me to make and substantiate by noting that the commercials have never failed to be the big net buyers on every day there has ever been a large silver sell-off. The confirmation of this can be seen in the Commitment of Traders and Bank Participation Reports. It is how the market works. Certainly, there can be no argument that every sudden price drop in silver has always benefitted the big commercial shorts. That shorts benefit from price crashes is beyond question. That these shorts intentionally caused the silver price crash is the outrage.

The concentrated commercial silver shorts deliberately pulled their bids on the COMEX in the past few days, like they have done countless times before, to force leveraged long traders to sell, so that the big commercial shorts could benefit. These big shorts are the only entities capable of withdrawing bids to cause such an impact. Therefore, they are the most likely traders to collude. They have the means, method, opportunity and motivation to collusively manipulate the COMEX silver market. This is not that complicated. It is also illegal as hell. It is a disgrace that big traders, banks no less, are allowed to openly manipulate the market. Why are banks allowed to speculate and manipulate the price of silver in the first place? What does the CFTC do all day that they don't see this?

How is it possible that we have allowed our market structures to develop with such serious flaws, in which the sudden removal of a few participants radically disrupts orderly pricing? In the case of the stock market, the resultant crash was most likely unintentional. It still needs to be remedied. In silver, the crash was clearly intentional. Not only does it need to be remedied, the big concentrated commercial shorts need to be prosecuted.

The CFTC recently received almost 3000 public comments pertaining to the silver manipulation and the concentrated short position. They did not receive 3000 public comments on the stock market crash. It is time for the Commission to address the will of the public on silver. The agency should immediately institute legitimate position limits in COMEX silver to break up the dominance of the concentrated commercial shorts. They should explain why that isn't the case and how allowing big banks like JPMorgan to dominate the market is good for society.

Chairman Gensler has now been in office for a year. While the problem predates his tenure, the silver manipulation has now become a crime in progress for his entire term. With a market crime this obvious, one day is too long; a year is an eternity. Gensler didn't waste much time appearing before Congress and initiating scrutiny of the flash crash in the stock market of May 6. This is how it should be. He hasn't spared any public words in condemnation of market concentration and the need for transparency and position limits. That is also proper. Now it is past time for him to terminate the never-ending flash crashes in COMEX silver and punish the manipulators. His responsibility is to protect his fellow citizens and the markets from fraud, abuse and manipulation. It is time for Chairman Gensler to stop talking about it and to take action.

Silver investors have been punished these past few days. The punishment shouldn't last long. Hopefully, not many leveraged positions, and no fully-paid-for positions were lost during this flash crash. That's the only effective antidote to what I believe is the ongoing criminal silver enterprise run by the CME Group and JPMorgan. More hopefully, investors were able to take advantage of the sharp price decline and actually add positions. This sell-off was intentional and engineered, and had nothing to do with anything other than artificially depressing the price to benefit the big concentrated shorts.

I know it may sound hollow and repetitive after another price smash, but this latest intentional takedown does greatly improve the market structure by eliminating as many of the leveraged long positions that were capable of being liquidated. The definition of the exact price bottom is when the last such long position is liquidated. No doubt we are much closer to that point, if not already there. It's just a shame and an outrage that the COMEX silver manipulation continues for even one more day.

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May 20, 2010

Date Created
2010/05/20