An Historic Vote<?xml:namespace prefix = o ns = "urn:schemas-microsoft-com:office:office" />

Since it largely followed expectations in Saturday's preview, I can't call yesterday's vote by the CFTC to approve position limits a surprise. But I sure can call it historic. For the first time in the 25+ years I have closely studied the silver market, we are facing, in the words of Commissioner Bart Chilton, a “new regime.” So radical is the potential change in the regulatory landscape that I must be mindful not to overstate the implications of pending hard position limits in silver.

The meeting itself was a bit flat (as I think was intended) and if you missed witnessing it live, please allow me to furnish the highlights. The vote, 3 to 2, followed along strict partisan political lines, with the two Republican commissioners objecting strongly to the measure. Commissioner Dunn provided to swing vote, joining Chairman Gensler and Commissioner Chilton to approve the staff's proposed formula for position limits. There was some disappointment in the final ruling, but there was much more for which to be encouraged. One quick note – I don't know what the short term impact might be on the silver market, as I'm sure both the regulators and the manipulators of silver want no big short term effect on price as a result of the vote. It would not surprise me if silver was kept under price pressure so as not to draw a connection to the vote. Then again, it would never surprise me if silver were to start to fly. That said, the long term implications for silver are exceedingly favorable because of the vote.

The disappointment was that the Commission completely ignored the thousands of public comments asking that 1500 contracts be adopted for speculative position limits in silver. The word "silver" was not mentioned once during the meeting, although there will probably be some mention of these comments when the full review is published in the Federal Register shortly. I assure you that 1500 contracts (7.5 million oz) is the correct level for position limits in silver and I doubt we will ever hear a legitimate debate to the contrary. After 20 years, I am not holding my breath that anyone will ever step up to the plate to engage in a legitimate debate on this matter. I am happy that the Commission voted to impose position limits, but not with their refusal to discuss the specific issues in silver. But we must be realistic – if they had adopted 1500 contracts as the silver limit (or even mentioned it), the world would have focused like a laser on why and that would have brought too much unwanted attention.

Another disappointment (albeit slight considering the realities), was the failure to identify JPMorgan as the silver manipulator that it surely is. One of the highlights of the meeting was Commissioner Chilton's opening speech, in which he alluded to manipulation as a result of a single trader holding a concentrated position of 30% to 40% of a market. Chilton amplified this theme in separate interviews before and after the meeting.

http://www.cftc.gov/PressRoom/SpeechesTestimony/chiltonstatement101811

I understand that commodity law precludes Commissioner Chilton or any other CFTC member or employee from publicly identifying any single trader's position. But I am an analyst relying on public data and I am aware of no restriction preventing me from identifying such a trader. Certainly, JPMorgan has never objected to my public identification of it being the big silver concentrated short, despite many opportunities to have done so. Specifically, JPMorgan held a high-water mark net short position of approximately 40,000 contracts (200 million oz) as recorded in the Bank Participation and Commitment of Traders Reports of December 1, 2009. That equaled 36% of the entire net COMEX silver market (excluding spreads) and almost 30% of the entire annual silver mine production at that time. This position was double JPM's concentrated short position of a year earlier and more than what Bear Stearns held when JPMorgan acquired them in March 2008. I assume this is the trader that Chilton is referring to, although I know he can't say so.

Away from these disappointments, there is much in the historic vote to be encouraged by. Most importantly, the Commission finally stood up to the biggest traders and the CME Group. This was no small accomplishment and reversed decades of the Commission being subservient to industry (to the public's detriment). In fact, this was at the center of all the divisiveness surrounding the contentious issue that position limits had become. The unspoken struggle to approve position limits was all about overcoming the CME's resistance. As I have previously written, this was particularly bizarre as the formula for position limits adopted by the Commission was first proposed by the CME Group itself. It was only after the CME and JPMorgan recognized that federally-mandated and administered position limits would threaten their market dominance and control that an organized resistance was mustered. Fortunately, that resistance failed in the end.

I know that many are now saying that the Commission's vote is only a temporary victory for the public and free markets and that court challenges are being prepared to reverse the move to a level playing field. This doesn't concern me too much as the merits for having federally-imposed position limits are so compelling that I doubt a further objective examination of the issue would favor the CME or JPMorgan. It comes down to who should set the boundaries of trading rules; an impartial arbiter like the CFTC or a conflicted (criminal) enterprise setting rules that favor its most influential members?

Lost in all the rhetoric about the great loss of liquidity, massive migration from our markets and increased costs that position limits will bring is the simple fact of how few is the number of traders that will be impacted by the position limits just passed by the Commission. Based upon the roughly 4400 contract limit (at current total open interest levels), take a wild guess as to how many traders would currently be affected in silver as a result of this limit. By my calculations, no more than one or possibly two traders on the short side and none on the long side would be impacted. The CME is going to go to court to protect the right of one trader, JPMorgan, to continue to manipulate the silver market? Good luck. (No, I don't really mean that).

It is only when you step back and view the past two or three decades of market and regulatory trends can you come to fully appreciate the significance of yesterday's vote. With one vote, admittedly too long in coming, the Commission has reversed the status quo of the largest traders always getting their way on everything. This is where history is being made. Up until yesterday, it was assumed by the majority that the exchange and the biggest traders knew what was best for the markets. It didn't matter, apparently, that everything that the exchange did was conflicted, from setting or refusing to set position limits that favored its biggest members, to allowing trade practices that had only one requirement increasing volume and revenue to the exchange. The amazing thing is that we all accepted this as being somehow legitimate. But it never was legitimate and yesterday's vote promises to set things straight.

Some are now fretting that the timeline for implementation is so stretched out as to make the vote meaningless. Same with JPMorgan being given exemptions from position limits for bona fide hedging. I don't see it that way. I don't think that the CFTC went through this historic and controversial change to let some manipulator sneak through the back door. Free markets often discount future events. I heard the same thing when Chairman Gensler started pressing for position limits two and a half years ago. At each mile marker on the way to legitimate position limits, it was always the same □ nothing would change. I'm sure Gensler doesn't look at it this way, but I do. Silver was $10 when he was nominated in December 2008 and $12 when he was confirmed in May 2009. It was $17 when Dodd-Frank was signed into law in July 2010. All along I heard nothing would ever be done and the price would reflect that nothing would be done. I think the record would suggest otherwise. Let me be clear □ I am not suggesting the CFTC is working to lift the price of silver; I am suggesting that any attempt to initiate fairness and logic in the trading rules will work against the decades' old manipulation that has been in place in silver.

I reserve the right to change my mind, but the reason I am not overly concerned about the timeline for imposing position limits is that the handwriting appears to be on the wall. Ironically, I think that the recent vicious and manipulative takedown in silver and gold was a direct result of the commercials on the COMEX realizing recently that position limits would pass, necessitating a manipulative move lower to really flush out leveraged longs. That illegal cleanout having been accomplished, the issue now turns to what happens next as a result of the vote.

The main takeaway to me is that the vote argues strongly against JPMorgan (or anyone else) ever building up a larger concentrated short position than it currently holds. Perhaps, as many believe, we get a further manipulative sell-off to flush out additional leveraged longs, but I'm not so sure. After all, current COT readings indicate a small potential number of longs left to liquidate. The bigger issue is that it's hard to visualize JPMorgan beefing up its concentrated short position from here. Without the ability to sell short unlimited quantities of additional silver contracts, the chief mechanism of the 25 year old manipulation may have just been rendered inoperative. At the very least, JPMorgan and the CME have got to be getting tired of being referred to as crooks and criminals. If so, that is a most bullish development for silver prices longer term. And long term is the correct term to focus on.

Short-term is anyone's guess (as always), but longer term it is hard to see any negatives for silver in yesterday's vote. For this day anyway, here's a tip of the hat to Gensler, Chilton and company. Not for a minute can we relax about the crooked shenanigans of the CME, JPMorgan and the other collusive commercials, with their HFT dirty tricks, but for today the passage of position limits should be celebrated for the achievement it represents.

Ted Butler

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Silver – $31.85

Gold – $1657