October 29, 2014 – Resolution is Dead Ahead

The Resolution is Dead Ahead

I've received several thought-provoking emails from subscribers that cut to the heart of the current situation in silver; so I thought I would summarize some common themes. Always the question of US Government involvement gets raised and, as time has progressed, I'm less inclined to argue against the idea. The manipulation has become so pronounced and has spread to so many markets that, at least from a knowing disregard perspective, the primary regulators (the CFTC and the CME Group) have to be culpable, as no one could be that clueless.

I still believe the main impediment to the regulators fulfilling their primary mission – preventing market manipulation Â? is by doing so now would heap shame and scorn on them for having failed to do so years earlier. Maybe there's some connection to protecting the dollar or the financial system, but how would I or anyone know that for sure? In any regard, the motive behind the regulators failure to regulate is not an issue for discussion today.

A number of readers did raise the more practical likely outcome to the current extreme market structure in COMEX silver (and the other COMEX/NYMEX metals). Most seemed resigned to a replay of what occurred on the two previous instances of extremely large technical fund short positions (into February and June) when the commercials (including JPMorgan) sold aggressively to technical fund buying and capped the silver rallies at no more than $3 each time. It's hard for me to argue with that predicted outcome, seeing as I'm the one who laid out the resolution alternatives and aggressive commercial selling was definitely one of those alternatives. Another alternative (still my personal favorite) is that the commercials may not be so aggressive the next time.

One reader, pointing out that I admitted to not knowing why the commercials let the technical funds off the hook so easy the last couple of go-arounds, suggested that the commercials were acting with no regard to a profit motive. I corrected him slightly, in pointing out that the commercials did profit on the last two occasions, turning significant open losses into adequate closed out gains, but had to admit it was much less than the commercials could have extracted if they pressed the technical funds to the wall. Still, his point was on the mark and if the technical funds do buy back current silver shorts near the current 50 day moving average (now close to $18) on a collective basis, then those funds will have succeeded in converting a large open profit into sizable realized profits.

If the technical funds were to succeed in buying back most of their silver short positions at a big profit, this would be a first and something I have declared impossible to the point of dressing up in a silly costume if it were to occur. I still feel that way, but considering how silver prices have flat-lined at lower prices, thus allowing the moving averages to drop notably; I am forced to admit that the technical funds are better positioned to convert open short sale profits in silver to realized profits than ever before. Will they pull it off? Let's discuss it.

While I did acknowledge to the subscriber that I still didn't understand completely why the commercials were so easy on the technical funds on the previous two occasions this year, at least I offered a possible explanation. Please know that I have thought of this constantly and I believe the explanation only comes into view when you think about silver through the manipulators' eyes (thinking like a criminal).

Since the commercials are so collusive and in control of the technical funds' trading activities, they can do with the technical funds as they see fit. I truly believe that the key to understanding the manipulation is to know that the commercials control everything that the technical funds do; just like a puppeteer controls a puppet. If it were otherwise, we wouldn't see the clear pattern in managed money behavior in silver (and other COMEX/NYMEX metals) of massive technical fund buying as prices rise and selling on declining prices, always ending in extreme positions at reversal points.

With this in mind, the only explanation that seems plausible to me as to why the commercials let the technical funds off the hook the last two occasions of extreme managed money shorting is because the commercials were biding their time and waiting for a more opportune time to put it to the technical funds. Let's face it, the technical funds have been like the goose that laid golden eggs for the commercials. You don't cook and eat a goose like that without a thought. What I'm saying is that the commercials know that they can maneuver the technical funds into any extreme position at any time they want and that earlier in the year the commercials let the technical funds off the hook because they knew they could do it again whenever the commercials desired. (That's my explanation, but if anyone has a different take, please drop me a note).

OK, let me anticipate your next question, namely, if they are in such complete control, why wouldn't the commercials do this forever? To answer that question, you must put your thinking on fast forward and look ahead. When you do that a terminal phase comes into view. The commercials, led by JPMorgan, have repeated this process in silver ever since the top in April 2011 at near $50. The big declines in silver have always featured aggressive technical fund selling. Over the last two years, in particular, the resulting desultory price pattern has encouraged more and more technical fund selling, culminating in the record short sales currently held in the managed money category.

But this marked increase in technical fund shorting has not come in a vacuum. Just like the derivative speculative take down in crude oil has important consequences, so too are there real world consequences in silver (and other COMEX/NYMEX metals). The glaring consequence of the rinse and repeat speculative take down in silver over the past few years is that the price has become stupid cheap. So much so that last week a leading silver miner proposed an illegal act to end the manipulation.

Because the price of silver is lower than could be reasonably imagined by the real supply/demand fundamentals, there must come an end the technical fund/commercial rinse and repeat. Look at it this way Â? if we get the same measly $3 rally this time in silver that we got twice before this year, the technical funds would be all done covering shorts and buying new longs at or below $20. If that were to occur (or if the technical funds bought even lower) the top of the next price cycle would still leave the price of silver below the primary cost of production. Then what Â? the down cycle is then repeated and we keep setting new successive lows in silver below any reasonable economic consideration?

At the very least, it would appear that silver needs to rally higher in this cycle than it did previously just to get it well above the primary cost of production, not something that had to be considered before this year. This manipulative pattern of futures trading dominating real world prices is increasingly coming into the collective view. That, alone, argues for the pattern to be broken. More importantly, a bigger silver rally on this go-around (or the next) would give the commercials more price room with which to maneuver the technical funds.

But there's something else that I've been thinking about recently. By not letting it rip to the upside in February and June of this year, the commercials certainly haven't lost anything in silver in that they have succeeded in getting the technical funds ultra-short again. Only this time, these same commercials appear to have maneuvered the technical funds in more markets than just silver (or gold). This time, there has been significant technical fund selling in all the COMEX/NYMEX metals Â? copper, platinum and palladium (as well as crude oil). Let me expand on this.

There was news this week that a single trader holds upwards of 50% of total LME copper warehouse inventories. Please be forewarned that I look at this with the intent of showing, once again, that futures trading on the COMEX exerts much more control over the price of copper than does even the LME news (which was widely reported) http://uk.reuters.com/article/2014/10/27/uk-lme-copper-redkite-stocks-idUKKBN0IG0PH20141027

For the sake of discussion, I will operate as if the news is completely accurate in order to make my point, even though I have no way of determining the goings-on at the LME myself (since there is so little transparency). With roughly 160,000 tons of copper in the LME warehouses, a 50% ownership would amount to 80,000 tons. All the news accounts focused in on this number and I would concede it looks like a formidable and newsworthy story. Except for one thing Â? it is very small and insignificant when measured against the futures position in COMEX copper.

This year I have increasingly mentioned how copper (and platinum, palladium, gold and even crude oil) has contracted the silver disease of having its price manipulated by excessive speculative activity on the COMEX. Specifically, I have zeroed in on technical fund positioning, or those traders included in the managed money category of the disaggregated Commitment of Traders Report (COT). In contrast to the published reports centering on the hedge fund Red Kite's position in LME copper inventories, the data in the COT reports is readily available and documentable and there is no need to rely on unidentified sources. The COT data, essentially, is accurate and available to all.

In the July 15 COT report and with the price of copper near $3.30 per pound, the net long position in the managed money category was nearly 49,000 contracts. In the October 7 COT report and with the price of copper having fallen nearly 10% to $3 per pound, the managed money category showed a net short position of more than 21,000 contracts. That is conclusive proof that technical funds sold 70,000 contracts net in COMEX copper futures and anyone can look it up (if you have trouble, drop me a line).

Since each contract covers 12.5 tons (25,000 lbs.), 70,000 contracts of COMEX copper are equal to 875,000 tons of copper. This amount is more than ten times the amount reportedly purchased by Red Kite. Yes, I know that COMEX contracts are derivatives and the reported purchase by Red Kite was for physicals, but I also know that the sale and short sale of 875,000 tons of copper derivatives in less than three months and by traders which only sell as prices decline was the cause for why copper fell. Over the past three months, there was no increase in world copper mining or supplies and no decrease in cooper demand as such changes are glacier-like in the speed with which they change.

The only conceivable and documented cause for the decline in copper prices was the concerted sale of 875,000 tons of copper futures contracts on the COMEX by the technical funds, an amount more than 5 times total LME inventories, the largest in the world. It is almost beside the point that these funds were tricked into selling by the collusive commercials, but this fact must be kept in mind. Now that copper prices look like they have bottomed, the extent of technical fund buying will determine the extent of the rally (which appears to have commenced).

I've been repeating this theme of technical fund selling of derivatives contracts as being behind the price drops in silver, gold, copper, platinum, palladium and crude oil because it has become increasingly obvious. The amounts are easily quantifiable and openly available. Not to bore you, but this entire process is so against commodity law and the purpose for why Congress allows regulated futures trading to exist that, at times, I feel I'm going insane. Either that, or the markets have taken leave of all common sense.

Regardless, this is something that also must be put on fast forward, as in Â? where the heck are we going with this process? Like something out of a Terminator movie Â? the computerized trading machines of the technical funds are battling it out with the collusive commercials to the point where the rest of the world is laid to waste. The excessive trading by speculative machines is dictating to the world's real commodity producers and consumers what prices they will pay and receive, even though the machines could care less. This is an evil development that must be changed. Sure, the consumers are favored now by the present too low prices, but if the cause is as I suspect, then that won't last for long. The world would be much better off if the uneconomic distortion of price by the speculative machines never existed in the first place.

The problem, in essence, is that the regulators (CFTC and CME) are allowing many separate traders (the technical funds) to trade as if they were one trader. The regulators would never allow one speculative trader to hold, long or short, 50,000 contracts of COMEX silver, or 100,000 contracts of COMEX gold or 70,000 contracts of COMEX copper because they know that would be manipulative to the price. Yet these same regulators see nothing wrong with allowing many different traders to act as one (thru the same computer signals) and having the same manipulative effect. The only solution, as I have outlined previously, is to treat the technical funds as the one trader they are behaving as and restrict their trading by collective position limits. But the chance of that occurring (and of having the regulators actually agree with me) is nil.

Instead, it looks increasingly to me like this war of the technical machines must have a violent ending, as that's the history of government action versus reaction. It's more likely that the technical fund/commercial control of the real world of commodity prices must have violent death to then be followed by regulatory Â?reforms.Â? At least, that's the way I see it.

What I think this means is that we are set up for violent price reversals to the upside for silver and for all the COMEX/NYMEX metals. Maybe the set up can get stretched out a little longer, but it looks stretched out enough to me by historical standards. We've gone too low in price on too many important commodities as a result of this stupid and manipulative machine trading. There's a payback and a counter-reaction to the price distortions we've witnessed and it seems to me that the payback is at hand.

I think the technical funds have been lulled into a sense of complacency, particularly in silver, by how easy the commercials have let them off the hook when they held extreme short positions recently. But just because the commercials have let the technical funds buy back shorts at prices close to upside penetrations of important moving averages previously, doesn't mean that will always be the case. Just because the technical funds think they will be able to buy back silver shorts near the $18 mark, that doesn't necessarily make it so. The commercials can demand much higher prices before selling. There will come a day when the commercials won't be nearly as accommodative to the technical funds as they had been previously and that will be a great day for silver investors. That day seems at hand to me.

Ted Butler

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Silver – $17.20

Gold – $1220

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