September 17, 2011 – Weekly Review

Weekly Review

In a market environment featuring large daily price swings, the price of both gold and silver fell for a second week. Gold was down about $47 (2.5%) for the week, with silver off 80 cents (1.9%). As a result of silver's slight outperformance, the gold/silver ratio tightened in a bit to almost 44.5 to 1, remaining near the top of a four month trading range. There wasn't much change in the year to date performance of each with gold up almost 28% and silver up 31%.

At this point, it still looks like the most plausible explanation for the great daily price volatility we are witnessing is the loss of true liquidity on the COMEX which I've written about recently. Particularly in gold, the unprecedented and aggressive short covering by the commercials to the upside since the beginning of August both explains the move to over $1900 and the volatile action in the recent chop. Certainly, there has been no other obvious explanation in the form of documented physical gold buying or selling that would justify the price action. In a nutshell, the retreat from the short side of the market by the COMEX commercials has drained liquidity to a point where any sizable order can move prices up or down sharply. Those conditions still exist. While this creates the environment for continued volatility, it also sets the stage for explosive price gains if, for instance, a true physical shortage were to hit (think silver).

In the physical world of silver, signs still abound of tightness on the wholesale level. COMEX warehouse movements appear frantic. That material has been moving in and out in massive quantities with little change in overall total warehouse levels suggest to me a struggle by someone to maintain an illusion of plenty even though actual metal may be tight. I know that sounds conspiratorial, but I just can't seem to rationalize it otherwise. There have been some additional deposits of metal into the big silver ETF, SLV, with total holdings at just over 320 million ounces. On the retail front, there does still seem to be some cooling off in demand for Silver Eagles (gold, too) from the white-hot pace of the past few years, although the US Mint will sell more silver coins this year than ever before. I also detect some cooling off in retail silver demand generally, based upon anecdotal feedback. I'm not particularly concerned with the current silver retail lull.

In my analysis, retail demand is important on a cumulative, rather than on an immediate basis. It is very significant that retail investors have gobbled up silver in the form of Eagles and other coins and bars to the tune of hundreds of millions of ounces over the past several years. Many little hands are the strongest hands of all. The massive cumulative purchase by retail silver investors is a cornerstone of real supply and demand. Yet the impact of retail buyer (or lack thereof) has little immediate impact on the daily silver price. That's because daily change in retail demand is small compared to daily changes in wholesale silver supply and demand. A case in point is that a few years ago there was a pronounced and obvious shortage of retail silver for many months, all while the price of silver fell sharply, thanks to COMEX shenanigans. A retail shortage or surplus is not enough to alter a wholesale shortage. Wholesale is what counts.

One factor in the wholesale category that counts a lot is the SLV, which holds the largest stockpile of silver on earth. And one factor in the SLV that I am most concerned with is the short position in its shares. As you know, I have tried to make a big deal this year about the short position in SLV because it grew alarmingly, up to almost 12% of all shares outstanding. I maintain that there is no silver deposited on shorted shares and because of the unique nature of this security (GLD as well) this represents a violation of what the prospectus promises. I consider shorted shares in SLV to be fraudulent and manipulative and that the Trust's sponsor, BlackRock, is negligent in its fiduciary responsibilities to shareholders for allowing the short position in SLV to exist. As such, I consider BlackRock, the world's largest asset manager, to be an enabler of the ongoing silver manipulation and anticipate the day when they will be held liable for damages.

The new short position for SLV didn't feature a dramatic increase, as it was up about 750,000 shares to just over 25.3 million shares(one share is equals one ounce), but it certainly wasn't lower (as it should have been). This marked the second fortnightly increase in the short position for SLV. Although the short position is down 30% from the peak level of near 37 million shares, 25.3 million is still so large as to be fraudulent and manipulative. We're still talking about a short position equal to 7.7% of total shares outstanding. That is obscenely large by any objective measure. http://www.shortsqueeze.com/?symbol=slv&submit=Short+Quote%99

More important is the practical effect this has on the price of silver. There are 25 million ounces held short in SLV; this is in addition to COMEX shorts, etc. The most plausible explanation (I know I am overusing the term) for why there are 25 million ounces held short in SLV is because the short sellers couldn't get hold of the 25 million ounces of real silver to deposit in the Trust, as dictated by the prospectus. It was easier for the shorts to not have to acquire the real metal and instead they gave a chit to the Trust, a promise to deliver real metal someday, just not today. Let me be clear Â? if the SLV shorts had to deliver real metal (as intended by the prospectus); given the current tight condition of the wholesale market, we would be over $60 in silver right now and possibly much higher. That's where the fraud and manipulation comes in; the SLV shorts are cheating all other SLV shareholders (of which I am one) and are distorting (manipulating) the price of silver. Sure, I'll send this to the CEO of BlackRock, Laurence Fink, but I doubt he will do anything until and unless it becomes a legal matter. Then why do it? Because he won't be able to claim he was unaware.

I know there is widespread distrust of the SLV by many. Just so there is no misunderstanding, I think the SLV is fine and the criticism is misplaced, except for this short business. If I change my mind I'll let you know.

This week's Commitment of Traders Report (COT) indicated expected reductions in the total net commercial short position in both COMEX gold and silver futures. I say expected because there were interim price declines during the reporting week of as much as $90 in gold and more than $2 in silver. The only reason we ever have sell-offs is because the commercials have rigged the market lower (via HFT and other tricks) precisely for the purpose of shaking leveraged longs out so that the commercials can buy. What was unexpected was the previous commercial buying on the big gold price rally.

In silver, the commercials bought back a total of 1900 contracts, pretty much evenly divided among the three commercial categories. The big 4 (read JPMorgan) bought back about 600 shorts, the 5 thru 8 about the same, and the raptors bought 700 new longs, increasing their long position to 2600 contracts. These are somewhat minor changes given the price volatility and may suggest not much additional liquidation ahead. For sure, there was additional speculative selling/commercial buying after the cut-off on Tuesday, as silver prices traded and closed below the 50 day moving average for the first time in two months on Thursday.

In gold, there was a more sizable 17,000 contract reduction in the commercial total net short position, leaving the commercials with their lowest short position since the COT of July 5. Somewhat unusual this week was that the gold raptors (the smaller commercials apart from the big 8) accounted for all the buying, having bought back almost 23,000 contracts of their short position. The big 4 added 4,000 gold shorts and the 5 thru 8 added around 1500 shorts. It is clear that the gold raptors were the prime factor in the gold sell-off during the reporting week. I guess they pulled the short straw in this week's commercial collusion contest.

From the high point in the total net commercial gold short of August 2, the position has dropped by 77,000 contracts (7.7 million ounces). The big 4 accounted for almost 15,000 contracts, the 5 thru 8 bought back 32,000 and the raptors bought back 30,000 contracts. This combined commercial buying took place first on the big upswing in price and then on the subsequent downward chops. The last time we were this low in the total commercial short position, the price of gold was under $1500. That we are $300 higher in price but are now back to a level in early July that I had labeled Â?spectacularly bullishÂ? (please check the archives) is somewhat remarkable. What does this mean?

I think it means continued volatility. In gold, the COT structure has to be considered bullish, just as it was back in early July. That augers well for a rally and against a prolonged liquidation sell-off. But conditions are notably different today in some regards. For one, the technical funds don't appear positioned to plow back onto the long side of COMEX gold futures at current or higher prices, having booked massive profits recently because they obviously felt the price was too high. I could easily see the tech funds buying gold after we go lower in price first down through the moving averages, with these funds then buying as the price reemerges through the averages to the upside. But we would first need a substantial price decline in gold for that to occur. On the other hand, the commercials do appear anxious to withdraw from the short side and after they get as much liquidation as they can manage on price declines, it's hard for me to see where selling pressure then comes.

I don't like to talk out of both sides of my mouth, but nothing would surprise me in gold because what we've seen to date is so unusual in the commercial buying to the upside. COT interpretations are just that Â? subjective opinions. From what we have experienced over the past few months, it's hard to speak with certainty. I can say with a high degree of conviction that we have suffered a dramatic loss of real liquidity. If big buying comes in on gold, we will fly in price. If big selling comes in, only continued commercial short covering will stem declines. Maybe we get a continuation of the volatile trading pattern within a fairly wide trading range.

I look at silver differently than gold. It will be volatile, but silver contains explosive upside potential that I don't presently see in gold (barring an outside development). The potential of a severe physical shortage in silver and not in gold is the main difference why I advocate a switch from gold to silver. The potential investment flow into silver versus gold is much more favorable than when I wrote about it back on March 30 (in the archives). As a result of the sharply higher price for gold since that date, the amount of money needed to sustain the gold price is much greater now, making it easier for silver to advance relative to gold. The silver COT structure is not wildly bullish, but it is much more bullish than it is bearish. Even though I study it with a microscope, there are more important potential influences at play in silver. Yes, if we sell-off, it will be because of crooked commercials games on the COMEX. I admit it would be better if I could pinpoint short term moves in advance, but I can't.

In terms of explosive potential factors in silver, I'd like to discuss two new developments this week. First, there was the news of a revised civil lawsuit being filed against JPMorgan for manipulating the price of silver. Although I am not directly involved in the suit, it closely follows the script I've written over the past few years. As such, you should know who I'm rooting for. There is no question in my mind as to which side should prevail, as I have been accusing JPMorgan of manipulating silver before anyone. In fact, I don't think there would even be a lawsuit if I hadn't first identified JPMorgan as the big concentrated short three years ago. But what I know to be true as an analyst is not the same as proving that in a court of law. That outcome is in the hands of the legal professionals on either side.

Still, I consider the lawsuit to be important in many ways. As is my habit, I'd like to discuss the case in ways I haven't seen discussed to date. My first observation is in regards to media coverage. Just like occurred when the lawsuits were first filed last fall, I was struck by the lack of media coverage and the spin on the story where it was reported. Make no mistake, this is a significant story. Manipulation is the most serious market crime of all, more serious than insider trading or even rogue trading. Silver is not an obscure security, but a widely followed market. JPMorgan is a master of the universe, not some minor financial player. Therefore, news of a lawsuit alleging a long term manipulation of a popular market by the likes of a JPMorgan should have the media in a reporting frenzy. Instead, the opposite occurred Â? there appeared to be a media embargo on the story. Why? Again, the most plausible explanation appears to me due to JPMorgan's financial relationship to the media.

There is no doubt that JPMorgan provides substantial revenue flow, in the form of advertising, to newspapers and broadcasters. Widespread coverage of a lawsuit alleging such a serious market crime would not be in JPMorgan's interest. Nor would it be in newspapers' and broadcasters' interest to lose advertising revenue. There was some spotty coverage in the Financial Times (of London) and the Wall Street Journal which ran an almost identical story (by different authors) which spun the story's importance as being HSBC's removal from the suit and not the significance of JPMorgan being named. It seems to me that JPMorgan has succeeded in burying the story, but the biggest shame rests on journalistic integrity. The story here is that there has been no legitimate story published.

The most significant fact in all this is that this lawsuit had been filed at all. Remember, this is a civil lawsuit. Market manipulation is a criminal offense and the regulators' number one mission and responsibility. There has never been before, to my knowledge, any civil lawsuit filed in a case that involved the manipulation of an important commodity before the government first filed charges of its own, either civil and/or criminal. I haven't seen anyone mention this. In other words, where the heck are the CFTC and/or the Justice Department? Has the state of regulation and criminal enforcement slumped so low that the private sector must intercede in the enforcement of the law? I am also struck with the silence from the CME Group. The civil lawsuit makes it quite clear that the alleged manipulation took place on the COMEX, which is owned by the CME. I have this crazy thought that the CME might be interested enough to comment on the most serious market charge possible. Crazier yet is the thought that they might investigate independently. Of course, that might interfere with their efforts to increase HFT capabilities.

Let me be very clear here Â? JPMorgan (and the CME Group) have not been found guilty of manipulating the silver market. But there are open allegations that they have manipulated the price of silver by me and now there are private lawsuits alleging JPMorgan has as well. The real story here is that the regulators who should be deciding this are missing in action. Let's resolve this important issue. If there is no manipulation, let's reach that finding. If there is and has been a manipulation, let's determine that as well and fix it. This is too important a matter for the CFTC to see, hear or speak no evil. It is shameful for the Commission to remain, literally, so out of it, while the public is clamoring for justice and private lawyers are filling in for the CFTC's Enforcement Division.

The other new development this week also concerns the CFTC. A scheduled public meeting for September 22 has been postponed to October 4. Presumably, this was the meeting at which the matter of position limits was to be decided. In addition, a disturbing story appeared that suggested great internal turmoil within the agency on this issue, replete with whistleblowers and the Inspector General. http://m.yahoo.com/w/news_america/exclusive-cftc-insiders-blow-whistle-position-limit-rule-165706682.html?orig_host_hdr=news.yahoo.com&.intl=us&.lang=en-us

I am not privy to what goes on within the Commission, but there is no question that the matter of position limits is a source of great contention. I have been petitioning the Commission and the exchange to adopt legitimate position limits in silver for 20 years, long before I started doing so on the Internet. That the issue of enacting position limits in the few commodities of finite supply that don't already have limits is so controversial is both surprising and not surprising to me.

I am surprised that it is so controversial because it is such a straight forward matter and has been a matter of black letter commodity law since the 1930's. Concentration is the root of all evil when it comes to manipulation, which is the regulators' primary mission to prevent. The only possible way to prevent concentration and, therefore, manipulation is by having legitimate speculative position limits in place. This is so basic as to question the motive of anyone opposed to position limits. Besides, we already have position limits in place for many commodities of finite supply, such as the grains and I am unaware of any call to remove them. What's the big deal about installing position limits in the energies and the metals? The proposed limits are so high as to only impact a handful of traders in every market. Yet position limits has turned into the most contentious matter of all. Why?

I have to speculate a bit here and you are forewarned that what comes next is my speculation. But, as in keeping with the thrust of this report, I'm talking about what is the most plausible explanation possible. The opposition to position limits and the turmoil it has caused is a false flag operation in my opinion. On the merits alone, position limits are good for our markets and good for almost everyone. There are no legitimate grounds for opposition. Those opposed to position limits are not telling the truth. What they are really opposed to are legitimate position limits in one market only and that market is silver. Silver is the only market with a manipulative concentration which legitimate position limits would undermine. But so extreme is the concentration on the short side of COMEX silver that specific and open debate on it is simply not possible. The only alternative for those opposed to ending the concentration in silver is to deal with it by not getting into a legitimate debate in the first place. Don't allow a fair and open debate on the silver concentration and position limits by characterizing the issue as something else, namely, a debate on position limits in general.

I think that is what's behind all the turmoil at the Commission on position limits. It isn't about position limits in general, it's only about silver, but no one can admit to that as the key is to not discuss silver in the hopes it will go away or be postponed indefinitely. You know, this is a common theme in silver, this don't dare utter that most vile of words. JPMorgan won't discuss it, even after being repeatedly and publicly accused and now sued. The CME won't discuss it, even though they are labeled a criminal enterprise. BlackRock won't go there either. Certainly the CFTC is in the same camp of ignoble silence in the face of an obvious crime. That three years have passed on the latest investigation with no comment is deplorable.

Only the public seems interested in discussing and resolving the matter. The good news is that, in the end, the public will prevail. We are at the point where a specific public debate on silver could happen shortly. Everyone but the public seems interested in keeping the matter of position limits and concentration in silver in the dark. But this is not an issue that is taboo. This is an issue that goes to the heart of the rule of law and what is fair. This is an issue that when openly discussed will result in substantially higher prices. We must continue to press for that fair and open debate.

Ted Butler

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Silver – $40.70

Gold – $1813

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