September 29, 2012 – Weekly Review

Weekly Review

For the second week in a row, the price of gold and silver finished mostly unchanged. This also had the effect of leaving the silver/gold ratio unchanged at just under 51.5 to 1. While the recent flattening of prices might suggest some type of free market equilibrium in play, a closer look under the hood indicates an extreme market structure destined to end with a violent move in price. The problem, at least for me, is in deciphering in which direction the price violence will occur; up or down. Or both.

Since yesterday marked the end of the month and the third quarter, I suppose I should note that gold and silver price performance were great on a monthly, quarterly and year to date basis, beating most comparable investment assets. But price performance over short time periods mean less to me than do the reasons behind the movements. As an analyst, I don't think I have ever suggested buying silver strictly because it may be going up at the time, as I am not a chart technician. I have suggested buying silver, of course, and that it would go up over the long term for many reasons; just not on upward price movement alone. Truth be told, there will come a time when the price of silver will be so high as to warrant saying good-bye to it as a long term investment. Regardless of short term price volatility, that time is still in the future.

Less than 24 hours ago, a federal judge ruled in favor of the banking industry in a lawsuit preventing speculative position limits from being enacted. I hadn't planned on writing about this, but obviously I will today. First, however, let me recount the week in the usual fashion.

The turnover in the COMEX silver warehouses continued, just as it has for the past year and a half. This week, total inventories rose by more than 2 million oz to 142 million oz, reversing lasts week's decline of nearly the same amount. That metal seems to be spinning in and out of the COMEX warehouses still indicates a tight supply situation from every angle I look at. Metal seems to be spinning into and out from the big silver ETF, SLV as well. After the delayed deposit of most of the silver I thought was ?owed? to the Trust (more than 10 million oz), nearly 4 million oz was withdrawn yesterday. Since there was no indication of investor selling, the most plausible explanation for the outflow was that the metal was needed more urgently elsewhere. From both COMEX and SLV (the two largest stockpiles of silver in the world) metal movement, supply looks tight.

Sales of both Silver and Gold Eagles from the US Mint hit the highest monthly totals since January, no doubt based upon retail demand responding to the upward price movement. Investment buying on higher prices is a fact of the collective human condition. More importantly, we are still on pace to witness the highest sales of silver relative to gold for any year in the Mint's 26 year history of the Eagle bullion coin program. Long term, this bodes well for silver.
http://www.usmint.gov/mint_programs/american_eagles/?action=sales&year=2012

The changes in this week's Commitment of Traders Report (COT) indicated an increase in the headline number in both gold and silver COMEX futures. As has been the case on past occasions, there was more to the story when digging down to the details.

In gold, the total commercial net short position expanded by 12,700 contracts to 262,400 contracts, the highest level since August 2011. Much more was revealed when studying the changes by commercial category. As was the case last week, the big 4 accounted for all the total commercial increase and then some, by shorting an additional 19,300 contracts. The gold raptors (the smaller commercials apart from the big 8) actually bought back (at a loss) 6300 contracts of their big net short position, the second buy back at a loss in as many weeks. Over the past few weeks, my sense was that the gold raptors rushed onto the short side very aggressively and early in the recent gold rally and may have left themselves vulnerable to buy back on further price gains. This is exactly what happened on the record run to $1900 in gold a year ago. I'm more convinced that my hunch was correct as the gold raptors have been buying back recently added shorts at a loss. I'm also more convinced than ever that the big 4 have come to the rescue for the raptors by shorting aggressively and keeping the gold price capped, thus averting even greater raptor short covering.

The proof of this collusive and manipulative behavior can be seen in the changes in the big 4's short position. It was only about six weeks ago that I was commenting on how the gold raptors were shorting aggressively, but that the big 4 was unusually light on the short side. Since that time, it has been, effectively, all big 4 short selling. From the COT of Aug 21, the total commercial net short position has increased by 90,000 contracts (9 million oz) and the big 4 have accounted for 80,000 of those contracts. Without that short sale of 80,000 contracts, the price of gold would have been higher by $100 or more; maybe a lot more if the gold raptors panicked without the intercession of the big 4. Just like in silver, this is an easy trail for the regulators at the CFTC and the CME to follow if either were remotely interested in rooting out manipulation.

In silver, it was the same old song with the big 4 (read JPMorgan) accounting for all of the increase of 1200 contracts in the total commercial net short position; now standing at 51,700 contracts, the highest since April 2011. The concentrated net short position of the big 4 is now 47,539 contracts (almost 240 million oz), the highest level since November 2010. I would calculate JPMorgan's concentrated net short position to now be 30,500 contracts (over 150 million oz). To help simplify my calculations (which I know confuse many), the COT report tells us that the big 4 are net short 47,539 contracts. That's a number you can take to the bank, as it comes from multiplying total open interest (133,163) by the 35.7% percentage held by the 4 largest shorts on a net basis. This is how one derives at net contract figures in the concentrated data section of any COT. Based upon my own propriety analysis, I am attributing JPMorgan as holding 30,500 contracts of the certain 47,539 contract figure. This leaves roughly 17,000 contracts held by the three remaining big 4 entities. If someone wants to disagree with my calculations (which is encouraged), the argument is in the portion I assign to JPMorgan and not in the big 4's position. Of course, one would assume that either JPMorgan or the CFTC would speak up if I were way off base.

Based upon my calculations, JPMorgan is still short 31% of the entire net COMEX open interest (minus spreads) and the big 4 hold a 48.4% share of the COMEX. I may come back to these percentages when discussing the lawsuit on position limits momentarily, but in any futures market such large concentrated market shares are clearly monopolistic and manipulative by their very existence. With the super concentrations now in place in both gold and silver on the short side, the COT market structure is flashing strong warnings of a sell-off, based upon past experiences. On the other hand, the physical silver market may be able to overcome the negative implications of the market structure. While I can't tell you which it will be, I can tell you that this COT structure versus physical conditions will be what determines the price of silver and not QE, currencies, politics or whether Europe or China fall into the sea.

As has been the case since I have followed the silver market closely, there are many positive factors in place that promise to send the price dramatically higher. And has also been the case, particularly over the past 4 years, there is only one negative factor and that factor is JPMorgan. A sharp sell-off will come if the crooks at JPMorgan get their way and with cooperation (collusion) from the other commercial jackals. I know there is no way that JPMorgan will be able to manipulate the price of silver indefinitely, but they may be crooked and powerful enough to pull off the sell-off scam one more time. I promise you that I would tell you if I knew which it would be. Not knowing, I'm still forced to play it on the basis of the long term inevitability of higher silver prices.

The big news is the ruling against the CFTC's move to implement position limits in the 28 physical commodities that didn't already have such limits.
http://www.reuters.com/article/2012/09/28/us-cftc-positionlimits-idUSBRE88R1C120120928
As long-time readers know, the issue of position limits in silver has occupied me for more than 20 years. Because it has been so long, I have a different perspective on the matter than most. Not better or worse than others necessarily, just different. Rather than rush to a snap conclusion as to what the ruling means, let me offer a Cliff's Notes summary of what led to yesterday's decision.

Following the financial crisis and concurrent large moves in oil and other commodities into 2008 and with the appointment of Gary Gensler as chairman of the CFTC in 2009, a process was undertaken to reestablish hard position limits in the physical commodities that had such limits in the past. At the center of concern were crude oil and other energy derivatives. In the crisis, you may recall, crude oil soared to almost $150 a barrel before plummeting to near $30. There was widespread belief that excessive speculation was behind the big price changes, even to the point of manipulation. Since the only effective means to prevent excessive speculation and the concentration that leads to price manipulation is to limit the size of speculative positions, Chairman Gensler spearheaded an effort to get position limits enacted where they did not exist. Commissioner Bart Chilton played an important role as well and the two of them seemed to be the only commissioners strongly advocating position limits to this day. Ultimately, position limits became a part of Dodd Frank, until they were derailed by yesterday's legal decision.

Quite separately and for a much longer period of time, I had been advocating position limits in silver as the only remedy (aside from a physical shortage) for ending a continuing price manipulation. For almost 20 years, the CFTC and the COMEX denied the need for position limits in silver and I have enough letters of denial from them to wallpaper a small room. As recently as May 2008 the Commission issued a public response denying a silver manipulation and the need for position limits. Therefore, I was quite taken back when the new chair of the agency started to proclaim in 2009 the need for position limits in all commodities. Let me correct that a bit, Gensler was concerned with position limits in energy, not silver. Further, Gensler, Chilton and Congress were concerned with higher energy prices, not lower. All were concerned with concentration and excessive speculation on the long side, not the short side.

But commodity law cannot discriminate between commodities and price direction; all commodities were eventually included in early proposals and it was not possible to just legislate against higher prices. So, silver got included in the position limit proposal and I began singing the praises of Gensler as the best chairman in CFTC history. I have since changed my mind as far as silver is concerned, as Gensler has presided over the biggest silver price smashes in commodity market history without lifting a finger or speaking a peep. Same for Chilton. These guys are supposed to protect the public and many regular silver investors have been decidedly unprotected in the manipulative silver price smashes. Sure, we were moving towards possible position limits in silver, but with such blatant price takedowns along the way that it mattered little. Besides, the Commission set position limits so high in silver compared to the thousands of repeated public comments recommending 1500 contracts that it was clear that the Commission and Gensler had little respect for the will of the people.

The real irony is that a delay in the enactment of position limits has little consequence to the markets everyone was concerned with at the outset of the process, the energies. That's because there is scant evidence of any pronounced concentration on either the long or short side in energy contracts. For instance, there is such a low level of concentration in the big NYMEX crude oil contract that the Commission's formula for the size of energy position limits hardly impacts any trader, according to COT concentration data. Since so few energy traders would be affected by the imposition of position limits as presently proposed, it makes you wonder why the industry group suing the agency and fronting for JPMorgan would even bother to oppose the measure.

I would contend that instead of looking at energy contracts as being the focal point of JPMorgan's opposition to position limits, look at where the actual concentration exists, namely silver and gold on the short side. In other words, the lawsuit was filed not because of concentration and the need for position limits in energy markets, but for the concentration on the short side of silver and gold. All the media reporting on this position limit story will focus, incorrectly, on the energy markets from the long side when the real story is in silver and gold on the short side.

JPMorgan would never come out and do or say anything to focus attention on their concentrated and manipulative short position in silver (and now gold). The whole purpose of the lawsuit was to delay the enactment of legitimate position limits in silver and gold. In this sense, the ruling yesterday must be considered a success for these manipulators in that they have stalled and delayed the movement to position limits. But this is temporary and only postpones the day of reckoning for JPMorgan for manipulating the price of silver. The securities industry group fronting for JPMorgan has admitted from the beginning and even after yesterday's ruling that they are not opposed to position limits, just not yet. There can be no doubt this was all about stalling.

Now it is up the Commission to decide how to proceed. They can appeal the ruling or start the whole process from the beginning, including the solicitation of public comments again. Either route will take time, assuming a Commission majority could even be attained. But there may be another way. A reading of the judge's decision rests upon the Commission failing to demonstrate the need for position limits in combating excessive speculation and manipulation. The need for position limits is elementary, despite the judge's ability to see it. However, there is a way for Gensler to easily demonstrate that need using the current circumstances in silver. This is not a new thought for me, although it came this time from a disinterested legal source. I don't know if Gensler (or Chilton) has the guts to pursue this route, but assuming Gensler means what he said about the continuing need for position limits yesterday, there may be an expeditious remedy at hand. http://www.cftc.gov/PressRoom/SpeechesTestimony/genslerstatement092812

It would be very easy for Gensler to show that JPMorgan is manipulating the price of silver by virtue of their 31% share of the market and the big 4 short concentration and market share of over 48%. After all, this comes from the Commission's own data. The problem is that Gensler is not a fighter by disposition and this allows him to get pushed around by JPMorgan and the other commercial crooks. Maybe others are correct in seeing him as being in cahoots with the crooks, but that's not the way I see it; he just isn't tough enough. While I didn't know the ruling was coming out yesterday and that it would shoot down position limits, I was going to comment on something now overshadowed by the decision.

This something was a very recent change in the behavior of the CFTC towards violations of speculative position limits on commodities where position limits were in effect, namely the agricultural commodities that had position limits all along. In little more than a week, the Enforcement Division has settled three separate cases involving violations of speculative position limits, including a $600,000 settlement with JPMorgan for violating speculative position limits in cotton futures. I can't remember a time when so many position limit cases were filed and settled. http://www.cftc.gov/PressRoom/PressReleases/EnforcementPressReleases/index.htmFor some reason, it appears that the agency may be flexing its muscles and maybe making a different point. Here's my speculation. Gensler knew how the decision yesterday would turn out for some time and was sending a message to JPMorgan and others that there would be consequences for stalling his position limit crusade. What better would explain the sudden rash of position limit violation settlements? If my speculation is anywhere near close, Gensler might be looking for a way to capitalize on the negative decision yesterday. If so, he needs to look no further than the concentration on the short side of silver (and gold).

As I have written in the past, Gensler (and Chilton) have something that few others have, namely, the power of the bully pulpit. Just a few choice words from him on silver could turn the stalled position limit process on its head. I even grant him to permission to use any of my comments as his own. For me to say that JPMorgan holds a 31% share of the silver market or that the big 4 hold a 48.4% market share is one thing, as I don't preach from any bully pulpit. For Gensler (or Chilton) to say it would turn everything completely upside down.

I know commodity law precludes any revelation of trader identity by the Commission, so JPMorgan needn't be identified by name; it would be enough for him to say a trader had a 31% market share and that was why we needed position limits. In that case, not only would the silver manipulation be quickly terminated, the path to position limits would be relatively instantaneous. As I said, I don't know if Gensler (or Chilton) is tough enough for such an approach or, for that matter, if he is as serious about the need for position limits as his public statements would indicate.

I do believe that much is swirling on position limits and JPMorgan's clear manipulation in silver behind the scenes. The stakes are very high and it is impossible to handicap the short term. I do remain convinced that the silver manipulation is on borrowed time and it is safest to count on the physical shortage being the final determinant. Still, it would be a sight to behold to see Gensler (or Chilton) man up for a change.

On a housekeeping note, a number of you have suggested that I make public the article on Wednesday dealing with the arguments against a silver manipulation under the premise that exposure would benefit us all. I'm inclined to agree, but I am mindful not to make too much public what subscribers pay for. I'm not doing it for marketing purposes but more to spread the word.

Ted Butler

September 29, 2012

Silver – $34.50

Gold – $1772

Date Created
2012/09/29