

August 20, 2010 – Hedge Funds in Review

Hedge Funds in Review

A quick word on market activity and then I'll close with a preview of today's COT report. Today's price smash in silver is, once again, the handiwork of the dominant commercials on the COMEX scamming the technical funds. It has nothing to do with real silver supply and demand and everything to do with forcing as many leveraged longs from the market as possible. As outrageous (and illegal) as this collusive commercial trading may be, and how negligent are the regulators for looking the other way, there is no doubt it improves the structure of the market. Let's face it; we can't prevent it in the short term, so we must deal with it objectively.

Silver has behaved much worse than gold over the past few weeks. Importantly, it is precisely this relative poor price action that sets the stage for a powerful silver price rally. Price bottoms in silver always coincide with there being little paper left to sell by the non-commercials. Such bottoms also always occur when we are below almost all the important moving averages, such as we are presently. The prospects for a price rally are always better when we are below key moving averages, like now. A thought I've had recently is that the poor price action in silver, especially when compared to gold, may be related to certain commercials knowing that the silver manipulation's end is in sight and there is a limited time to position for what's to come. The price action suggests to me that these commercials are more concerned with silver than they are with gold. I also have the strong feeling (admittedly as I've had before) that the next rally will be the big one for silver. Considering the position limit regulatory process under way, it's hard for me to imagine the silver scam lasting much longer.

There was some significant news in the hedge fund world this past week. (I'm speaking of the big macro-economic hedge funds, not the technical funds that trade on the COMEX.) For one thing, the list of holdings for the big hedge funds was released for the end of the second quarter. As of June 30, there was a notable addition to the already sizable holdings in the big gold ETF, GLD, and gold mining securities by these big funds. A back-of-the-envelope calculation indicates that the big well-known funds own close to 20% of GLD, or \$10 billion worth, plus billions more in gold mining shares. I'd like to contrast that with what the big hedge funds (not index funds) own in SLV or silver mining shares. To my knowledge, the big hedge funds (like Paulson, Soros, et al) don't own any SLV or silver mining shares. I'd like to make the observation that while some are concerned that selling by these funds might someday pressure gold prices, such fears don't exist in silver. Further, the beneficial impact on gold prices of the hedge funds' purchases to date has already been felt. Since they haven't bought any silver yet, no impact on price has occurred. If they do decide to buy silver in the future, the impact on price will be felt then.

The other hedge fund news of the week was the announcement that Stanley Druckenmiller was closing down Duquesne Capital, the hedge fund he founded 30 years ago. Mr. Druckenmiller's fund was highly successful and up until the last couple of years, had enjoyed consistent annual returns of 30%, in the process making him very wealthy. From everything I've read over the years, Druckenmiller was the real deal, not just a superb money manager, but also a hand's on philanthropist and devoted family man. If you're guessing that I hold him in high esteem (even though I don't know him), you would be correct. Perhaps you might remember Mr. Druckenmiller's currency play for the Soros fund that netted a billion dollars on the British Pound. That episode, back in 1992, brought out one of his most memorable investment lessons, namely, when you are sure you are correct, bet big.

Druckenmiller gave as his chief reasons for resigning from investment management as the difficulty in managing large sums of money, as his fund held \$12 billion in assets and in finding good investment ideas. The reason I'm writing about Mr. Druckenmiller and the hedge funds are that I'm convinced that silver is the most spectacular investment idea of all time. I'm struck by the fact that no big hedge fund has yet to discover it. I can only assume that silver, for some reason, never made it to their radar screen. You won't see, if don't look. This is something that will surely be resolved in time. Here we have a vast pool of money looking for a great investment idea and that great investment idea existing in silver. Someday, that connection will be made and the results will be evident in the silver price.

That connection might come sooner as new articles appear highlighting the silver manipulation. Here's one from a gentleman I mentioned in my last article, Ben Davies from Hinde Capital. http://www.hindecapital.com/docs/hil_reports/HindeSight%20Investor%20Letter%20August%202010.pdf

In addition to appreciating Mr. Davies kind mention of my work, I believe it is important that the allegations of silver manipulation be fully aired. As I've written previously, it's hard for me to take any analysis of silver seriously, that doesn't feature the concentrated short position on the COMEX.

Finally, I'm not sure what to expect in today's COT report. I know silver is in better shape than gold, market structure-wise, and that the rotten price action since Tuesday's cut-off has improved the silver structure. But I have questions in my mind about today's report. The report today will include a big increase in gross total open interest (that's easy to predict). The question is if the increase in total open interest includes a big increase in commercial short selling, especially by the big 4 (JPMorgan). Alternatively, the big increase in total open interest could be related to an increase in spread positions, which is not of a concern. I guess I'm hopeful that the increase in total open interest does not represent an increase in short selling by JPMorgan, breaking their recent pattern of reducing their silver shorts. Considering how weak silver prices have been this week, if it does turn out that JPMorgan increased their short position that would be about the clearest proof possible that they are manipulating the price of silver. I'm sure I'll be discussing this when King World News interviews me later, for release tomorrow.

Ted Butler

August 20, 2010

Silver – \$17.97

Gold – \$1227

Date Created

2010/08/20