

February 11, 2012 – Weekly Review

Weekly Review

For the second week in a row, the price of gold and silver finished marginally lower, especially when measured in percentage terms. Gold was down about \$5 for the week, with silver down almost 20 cents. As a result of the basically flat relative performance, the gold/silver ratio remained in the same low 51 to 1 range it has traded in over the past two weeks. Year to date, gold is up 10% and silver is up 20%. There were some real crosscurrents in developments beneath the surface and I'll get to those as I review the usual weekly mileposts.

Conditions in the physical silver wholesale market still appear tight. The torrid daily pace of material into and out from the COMEX-approved silver warehouses abated only slightly, as total inventories declined slightly to just over the 129 million ounce level. The turnover still remains a more important indicator of tightness to me than does the total level of inventories. Inflows of metal into the big silver ETF, SLV, continued with total deposits now totaling over 6 million oz over the past two weeks. Additionally, the Sprott organization has begun receiving metal on its approximately ten million ounce recent purchase for its own ETF, PSLV. Finally, the Swiss silver ETF, ZKB, has added 2 million silver oz over the last fortnight. All this actual metal activity adds to and confirms tight physical conditions in silver.

A quick word on the recent reduction in margin requirements for COMEX silver and gold futures contracts, which several of you have asked about. On balance, this is much ado about nothing. Reducing initial margin requirements on a silver contract from close to \$25,000 to \$21,600 doesn't change much. A silver contract is currently worth a nominal \$170,000 and dropping (or increasing) margins by a few thousand dollars won't induce much change in market structure or participation. Margins exist for one basic purpose – to protect the broker and the clearinghouse. It is quite true that the series of silver margin increases starting last May did help to kick silver down the price stairs (as intended by the CME and the collusive commercials). However, that's a dirty trick that the crooks can only pull out of their tool kit every once in a long while. Given current conditions, changes in margin requirements are not terribly important. Someday maybe, just not right now.

The first big development this week is one that caught me by surprise, although perhaps I shouldn't have been completely surprised. I'm speaking of the new report on the short position in shares of SLV, as of the close of business January 31. Where I was girding for an increase in the short SLV position (since we climbed nearly \$4 in price for the two week reporting period), instead there was a very big decline in the short position of more than 35%. The short position in SLV declined by 9.4 million shares (ounces), from 26.6 million to under 17.2 million shares. This is the biggest two-week reduction in the SLV short position in my memory and the first I can recall when silver prices were advancing. The decline in the SLV short position brings it down almost 50% from the high-water mark of over 36 million shares in the spring of 2011. <http://www.shortsqueeze.com/?symbol=slv&submit=Short+Quote%99>

I admit to doing a double-take when I first glanced at the numbers. As I previously reported, towards the end of December, I received a very threatening letter from lawyers representing BlackRock, the sponsor of the SLV, demanding that I cease defaming their client on the shorting SLV issue. By coincidence, on the same day I received the letter, I got a call from a fellow subscriber and friend (who is a European money manager) and when I told him about the letter, he told me that it probably meant that BlackRock was taking this very seriously and would move to get the SLV short position reduced, despite the threatening tone of the letter to me. I told my friend that I thought (and hoped) that he was correct and we would see if we were correct in future short reports as they were released.

I can't help but feel that the most plausible explanation for the dramatic reduction in the SLV short position (especially on rising prices) is as my European friend predicted, namely, that BlackRock came to realize that the shorting of SLV was fraudulent and manipulative and they are working to eliminate it. Of course, I don't want to be overly optimistic and if we witness future big increases in the short position of SLV that would indicate we were back to the old fraud and manipulation in the shorting of those shares. But let's take it one day at a time and reserve judgment on whether we go back to the bad old ways of short selling in SLV.

I fully admit to "owning" the SLV short selling issue, for better or for worse. I've identified it as one of two key issues for the future price of silver (along with JPMorgan's concentrated COMEX short position). The SLV short position can still increase substantially in the future and, if it does, it will continue to draw the attention from me that it fully deserves. But if the SLV short position does not increase big from here on out, that would be very good news indeed. That's because no big future SLV short increase would indicate that the crooked silver shorts have abandoned using a powerful tool they have used in the past to cap the price of silver. I don't want to get carried away here with rosy scenarios (wait until I get to the COT discussion), but there is another aspect to this reduction in the SLV short position that bears mentioning.

If, as my European friend has suggested to me, BlackRock did get the message and has moved to pressure the SLV shorts, it means that you writing to them may have made the difference. Please think about that in terms of writing to the CFTC and your elected officials about the 3.5 year investigation into silver. I know many say that it is futile to write because it does no good. To that I say nonsense. The proof is in the ongoing investigation itself, as there would be no investigation if people didn't write in initially. That BlackRock may have worked behind the scenes to reduce the SLV short position while appearing openly to bite off my head should be additional encouragement to press forward on contacting elected officials on the CFTC's silver investigation.

Away from the apparent good news on the SLV short position, the news wasn't so great in this week's Commitment of Traders Report (COT). There was a continued increase in the headline number, the total commercial net short position, in both gold and silver. The total commercial net short position reached its highest level in each for the current price move higher. It wasn't that the price gains were so large during the reporting week; it was more a case that the gains took us to new price highs for the year to date. Marginal new price highs tend to excite and cause technical traders to buy on those new highs.

In gold, the commercial net short position grew by 11,200 contracts to just over 221,000 contracts. It was mostly a case of the big 4 and the gold raptors doing the majority of the selling. The big 4 sold a bit over 5000 additional contracts short and the gold raptors selling almost the same amount, increasing the raptors net short position to 25,300 contracts. (Last week I botched up the gold raptors position a bit, as a subscriber pointed out).

In silver, the total commercial net short position grew by 5900 contracts to 34,700 contracts. The big 4 (read JPMorgan) sold an additional 1300 contracts short, with the silver raptors (the smaller commercials apart from the 8 largest commercial traders) selling 4000 of their longs, reducing their net long position to 8200 contracts. The new price highs during the reporting week did draw new technical fund longs into the market, which had not been the case until the past couple of weeks.

The monthly Bank Participation Report, along with the weekly COT, suggested to me that JPMorgan's concentrated net short silver position is now close to 19,000 contracts, or the equivalent of 95 million ounces. This represents an increase of close to 6,000 contracts in JPM's silver short position since late December. If the reduction in the SLV short position was good news in that it suggested a potential end to that manipulative mechanism, the increase in JPM's short position on the COMEX suggest the manipulation is alive and well. I can't help but think that the big reduction of 9.4 million oz in the SLV short position didn't buoy silver prices much higher precisely because there was much more new selling on the COMEX. In fact, I would not be surprised if JPMorgan was simultaneously buying SLV shorts back while selling new short COMEX contracts in a brazen attempt to control prices.

I think it would be instructive to step back view the landscape from the bottom in prices at the end of December and the COT market structure in place at that time, to where we are today in gold and silver. In gold, on close to a \$250 rally, the speculators bought and the commercials sold close to 60,000 net COMEX contracts (6 million paper oz). In silver, on close to an \$8 rally, the speculators bought and the commercials sold just over 20,000 net contracts (100 million oz).

Six million COMEX paper gold ounces is a very large amount of gold, much larger than any other documented purchase and sale of gold in any other venue, including cumulative changes in gold ETFs. One hundred million ounces of silver is an absolutely gargantuan amount of equivalent metal that changed hands on the COMEX over the past 6 weeks or so. My point is simple — since the net change on the COMEX in gold and silver holdings was much larger than any other verifiable exchange of gold or silver, it was this net COMEX change that was responsible for the price of each rising over the past 6 weeks. Commodity law holds that futures markets shouldn't set the price for world commodities. Yet CFTC data show this is exactly what happened and is usually the case.

The price of any investment vehicle goes up or down based upon whether the buyers or sellers are the initiators of the transaction. It's not whether there are more buyers than sellers, or vice versa, that moves prices, because there has to be a buyer and a seller in each and every transaction. What matters is who is more aggressive, the buyers or the sellers. Simply put, if prices are moving higher, it means the buyers are more aggressive or are willing to reach and buy at higher prices. If prices are falling, it means the sellers are more anxious to sell and will do so at lower prices. This is true in every market. Therefore, this means that over the past 6 weeks or so, it has been the buyers who have been the aggressors in COMEX gold and silver. According to government COT data, the buyers in gold and silver have been the speculators. The commercials have clearly been the sellers according to that same data.

So if the speculators have been the buyers on the COMEX and are responsible for the price rise, where do I get off in labeling the commercials as the crooks? After all, the commercials have been selling on this price rally, not buying. The answer is that the measurement from the end of December is not the right measurement. It happens to seem logical to start at that bottom and COT structure and I just did so above. But it is not the right point to measure from in terms of whether silver is manipulated or not. That's because the price bottom at the end of December and the extremely bullish COT structure at that time did not come about through free market developments or even by accident. We arrived at that extreme set up at the end of December only by collusive and manipulative action on the part of the commercials. These commercials while few in number (15 to 20) have a such a disproportionate dominance over gold and silver pricing on a day to day basis that they can lead the speculators into and out of the market. The commercials have numerous tricks up their sleeves, such as HFT and knowing how the speculators will behave at all price levels. This can only be done through collusion.

I've commented in the past about how the scam that the COMEX commercials have going is close to the perfect crime. This is what has permitted the silver manipulation to last as long as it has. By colluding amongst themselves, the commercials always buy on lower prices and sell on higher prices. That gives them the perfect cover. So, even though they are rigging prices lower and higher at will, because they are always buying on lower prices and selling on higher prices, these commercials can always say to the regulators (if the regulators ever ask), "What are you bothering us for? We bought on that big price decline and sold on that big price rally. You should be thanking us for making markets." These commercials shouldn't be thanked, but put out of business (and perhaps in jail). That's because it is impossible, in a free market, for them to always be on the right side. That's a question the regulators never seem to ask, namely, how can these commercials nearly always be on the right side? The answer is because they control the market.

OK, what's the bottom line with all this? Compared to where we were at the end of December, price-wise and in terms of COT structure, we are nowhere near as good now as we were then for a price rise. Does this mean we could sell-off? Yes, we could. Does this mean we must sell-off? Not necessarily. While the current COT structure is not as constructive as it was in December, there have been plenty of occasions where we charged higher in price with much worse COT structures than currently exist.

For instance, exactly one year ago, we had a much more negative COT reading in silver than we do now, yet silver exploded over a few months to near \$50. Later, in gold, the commercials sold aggressively in August and were forced to buy back at much higher prices on the move over \$1900. We did have close to drop-dead bottoms in December and I hope I conveyed that to you at that time. We are not at similar extremes in COT terms now, but that doesn't mean we can't go much higher in the price of silver on other considerations, such as physical market developments.

I think it comes down to a question of individual long term expectations. Over the past year and half or so, I have been hesitant to suggest anyone abandon long term silver positions, even when COT readings have been much worse than currently. That's because I'd rather take a temporary smack down in price than risk missing the big run the upside. Given the long term risk reward ratio in silver, the worst possible thing would be watching the silver rocket take off and not be onboard. Quite frankly, that scares me more than anything. The big moves to the upside so far have come with negative COT readings (save for the move since December). Chances are that the monster silver move to come will develop when something goes wrong for JPMorgan and the commercials in general will be not in the COT position they wish to be in.

It's important to remember that silver, like any market, is similar to a three-ring circus, only with more rings. You remember the circus and all the different activities; clowns, trapeze artists, the elephant parade and the man being shot out of the cannon. So much going on, all at once. Same thing in silver; physical movements, COMEX COT changes, the SLV short drama, the wait until the CFTC gets some backbone and what JPMorgan is up to. If you study one aspect too closely, another important development can catch you out of position. The trick is to stay balanced. Don't be in a position to be forced to sell if prices drop (no margin), but don't be too lightly positioned if we take off. And don't forget to write to your congressman or senator about the unnecessarily prolonged CFTC silver investigation. It has and will make a difference.

Ted Butler

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Silver – \$33.50

Gold – \$1720

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