February 18, 2012 – Weekly Review

Weekly Review

The price of gold and silver were mixed for the week. Gold was up about $5, with silver down about 25 cents; both changes marginal in percentage terms. Basically, the price of each has been little changed for the past three weeks, after having started the New Year strongly to the upside. As a result of gold's outperformance this week, the gold/silver ratio widened out to near 52 to1. Since year end, silver is still up relative to gold.

Conditions in the wholesale physical silver market still appear tight, although retail demand may be cooling off. There is still unusually high turnover or movement of metal into and out from the COMEX approved silver warehouses, as the total level of inventory was mostly unchanged for the week. Although there is little sign of widespread attention to this silver movement, it still resonates with me. That's because, up until a year or so ago, such consistent turnover didn't exist.

The vision of daily large truck deliveries, being loaded and unloaded in and around New York City (not the most traffic-friendly environment) is one I often think about. Having some familiarity with that NYC traffic, I can't help but ask- who would subject themselves to that experience unnecessarily? What is so important about moving metal so feverously in those traffic conditions and congestion? The most plausible explanation to me is that most of the near 130 million oz already there is unavailable and new stuff must be brought in to satisfy consistent withdrawal demands. Again, this turnover pattern didn't exist over the past quarter century.

Sure, there were times over the past 25 years when many tens of millions and even a hundred million oz came into and out from the COMEX silver warehouses over varying periods of time. But I don't ever remember this daily in and out on the COMEX. I admit to being on alert for any different or unusual patterns that may develop that are different than in the past. I suppose that's normal in analyzing any market, but there's more to it in my case. I confess to being convinced that the silver market is crooked to its core and, therefore, being extra alert to any different pattern that may signal the end of the corruption and the freeing of the price. Being also convinced that physical tightness will eventually trump the manipulation, I am particularly sensitive to any suggestion of physical tightness. This consistent physical turnover in COMEX silver looks like tightness to me. Humor me Â? if you have any other explanations, drop me a line.

Also adding to the signs of physical tightness was the withdrawal of 3.5 million oz from the big silver ETF, SLV, this week. Price patterns and trading volume did not suggest that the withdrawal was due to plain-vanilla investor liquidation. The most plausible explanation was that SLV shares were converted to metal and that metal was removed because it was needed somewhere more urgently than in the London warehouse of the custodian. This tends to confirm the tightness scenario, as does the 600 thousand oz withdrawal from the big Swiss silver ETF, ZKB.

One place receiving silver recently was the Sprott silver ETF, PSLV. Ed Steer reported this week, after a conversation with Eric Sprott that all the 10 million oz recently purchased in the public offering had been received. This was even sooner than I had speculated about a month ago. I had anticipated the metal would be received quickly because Sprott would likely make public any delay in getting the silver and announce how tight the physical market was. The big commercial interests who have been manipulating the price were not likely to allow that to occur. My point, which I will also make later, is that more often than not, it is best to view the silver market from the perspective that it is corrupt and artificially depressed in price by big commercial entities. Things become more understandable as a result.

On the retail front, demand seems to have cooled off very recently, based upon anecdotal evidence and reports from the US Mint. I think I recently reported some fears of mine on this occurring. The Mint can sometimes report sales erratically, but February sales for Eagle bullion coins are off sharply for the month to date. Silver Eagle sales are still more than holding their own compared to Gold Eagle sales, but both are off sharply from recent levels. You want to be circumspect in analyzing the data. Silver Eagle sales have been blowing off the roof for years and will likely do so again in the future, due to the coin being such a great way to own silver. But every market gets fatigued and stale at times, especially after a long and blistering sales pace. The cooling off coincides with silver (and gold) prices very recently flat-lining. Investors love a bargain or higher prices; flat prices are like kissing your sister, not good and not bad. (My two sisters excepted, of course).

One thing I can tell you with some degree of certainty is that the recent lackluster retail demand and sales of Silver Eagles do not impact the wholesale price to any great extent. For one thing, the Mint is still producing near the same quantity of Silver Eagles as they have struggled to keep up with demand for years. I would imagine the Mint would like to build up a bit of a silver inventory cushion to prepare for future surges in demand for Silver Eagles. Also, if the current cooling in demand persists, the Mint can address and prepare for lines of proof silver coin production curtailed in recent years. In terms of important influences on the near term price of silver, one must look away from retail demand and Silver Eagle sales. Instead, look towards the COMEX.

A quick response to a reader question involving Silver Eagles and world silver inventories, before turning to the COTs. Stan asked me, among other things, if I was overlooking the amount of Silver Eagles and other coins in my estimate of total world silver inventories of around a billion ounces. The answer is yes, but intentionally so. I try to be careful in stating world silver inventories in terms of bullion only, or bullion equivalent. I also try to be careful when I compare the level of total world silver bullion inventories to gold bullion inventories, sometimes to a fault. When I use the word bullion in silver, I'm talking about silver in the form of 1000 oz bars, the industry standard. In gold, the industry standard for bullion is 400 oz bars, but that distinction is not as important as it is in silver. That's because industrial demand is more important in the silver supply/demand equation than it is in gold.

I don't consider the 250 million oz of Silver Eagles cumulatively produced and sold by the US Mint over the 26-year life of the program to be part of the total world silver bullion inventory. Nor would I include previous coinage programs or other forms of non-1000 oz bars of silver. Certainly, silver is silver and Silver Eagle and other coins are silver. However, I analyze silver as I would any world commodity, namely, from a most likely total supply/demand perspective. Silver has an important industrial consumption component (that is largely lacking in gold). A key factor in my analysis is that there will likely be an eventual rush by industrial silver users to stockpile inventory. The inventory rush will be for 1000 oz bars.

Of the 250 million Silver Eagles coins produced over the past quarter century, my guess is that not a single coin was melted for its silver content. That's because Silver Eagles have never sold for a big enough discount to the price of silver to justify melting. Surely, plenty of Silver Eagles have been bought and sold over the years, but sellers have never had to resort to melting to extract value; other investors have purchased whatever has been sold. Other silver coins, especially those termed Â?junkÂ? (pre-1964 circulated coinage) have been melted, but that previous melting has greatly reduced the remaining amount that could still be melted. Nowadays, bags of junk coins are more likely sold to a new buyer rather than ending up at a refiner.
An additional factor is that Silver Eagles and other coins are generally held in very diverse hands, making the acquisition of large quantities difficult at best. Silver industrial users won't be rushing to buy Silver Eagles, but 1000 oz bars.

Of course, conditions can change in the future and if it becomes clear that Silver Eagles and other forms of silver are being melted, I will have to include that in the analytical mix. For now, I don't include Silver Eagles in bullion inventory totals. Thanks for a great question, Stan.

The changes in this week's Commitment of Traders Report (COT) were mixed for gold and silver. The headline number, the total commercial net short position, decreased in gold and increased in silver. Prices during the reporting week finished mostly lower every day in each, with gold declining about $25 and silver by as much as a dollar, although silver did hit new intraday highs for the current move early in the reporting week.

In gold, the total commercial net short position declined by 11,700 contracts to 209,400 contracts. By category, the big 4 bought back about 4600 of their net shorts, while the raptors (the smaller commercials apart from the big 8) bought back 6,000 of their shorts, reducing their net short position to 19,300 contracts. The 5 thru 8 accounted for the balance. As is usually the case, the gold commercials behaved in conformity in buying from the speculators on lower prices.

From a market structure basis, the gold COT is neutral (as is now silver) based upon recent COT parameters. We're at the point where nothing should surprise you price-wise. We are no longer at the very bullish readings of late December, but neither are we at what could be called very bearish COT levels. Are we at COT levels where the commercials have smacked down prices previously? Yes, sometimes the commercials have smashed prices from these equivalent COT readings. On the other hand, similar levels of previous COT levels have resulted in shocking gains, particularly in silver. I want to tell you how it will play out this time, but the truth is that I can't.

In silver, the total commercial net short position increased by 2700 contracts, to 37,300 contracts, the highest level since the COT of September 20 (just before the late September manipulative price smash). By category, the big 4 (read JPMorgan) sold an additional 1600 contracts short, increasing their net short position to 36,915 contracts, also the highest level since September 20. The raptors sold 1200 contracts of their net long position, reducing that net long to 7,000 contracts. The raptors now hold their smallest net long position since (as you may have guessed) September 20. This is definitely not coincidental, but indicates collusion among the COMEX commercial traders.

If I can't tell you the immediate direction of prices, at least I can describe what is going on in broader terms. It has been no surprise to me that silver and gold prices have risen strongly from the late-December dramatic lows, given the extreme COT readings then. At that time, the commercials had succeeded in artificially rigging gold and silver prices lower to force selling by the speculators. This allowed the raptors to increase their net long position in silver to the highest level in years. It also allowed JPMorgan the opportunity to reduce its net short silver position on the COMEX to the lowest level since acquiring the concentrated short position from Bear Stearns almost 4 years ago.

At that time in late December, it appeared to many that the price of silver and gold would continue to collapse in the manner they had been declining and that JPMorgan would continue to reduce its short position and possibly even get net long silver for the very first time. While acknowledging that this was possible, I remained doubtful that JPMorgan could achieve getting net long silver, mainly because it looked to me like the market was close to running out of the requisite reciprocal speculative selling necessary for JPM to buy that many contracts. As it turned out, I was completely correct. But then I made a prediction that was as wrong as could be possible. I then predicted that JPMorgan, having achieved the truly remarkable feat of reducing their net short COMEX silver position to around 13,000 contracts (65 million oz), would finally wash its hands of the silver manipulation and would never meaningfully increase that concentrated short position again. Hey, at least I wasn't wrong by a little bit.

Based upon the latest COT report, JPMorgan appears to be now net short almost 21,000 contracts (105 million oz) or more than 60% (40 million oz) more than they were short on December 20. In the COT report of December 20, the big 4 were net short 28,023 contracts and my guess was that JPMorgan held 13,000 contracts of that amount. As I indicated above, the net short position of the big 4 in the new report is 36,915 contracts, or an increase of 8892 contracts. I think JPMorgan is responsible for 90% of the increase in the big 4 concentrated net short position and I would like to explain what that may mean in broader terms.

Please remember that I am speaking of the concentrated short position. That basically excludes the raptors which haven't been net short recently anyway. I think the raptors are colluding to manipulate the price of silver, but in a manner different than JPMorgan, which is doing so by virtue of a singular dominant position that has the effect of controlling prices. And it makes little difference, in a legal sense, whether JPMorgan holds this position by itself to the extent I suggest, or whether the other three entities in the big 4 are colluding with JPMorgan to manipulate the price of silver. That's the essence of collusion. Besides if numbers are off and JPMorgan wants to set the record straight about its silver short position, let them do so, as no one is stopping them.

The clear fact is that had not JPMorgan sold short 40 million ounces of the almost 45 million oz sold by the big 4 since December 20, the price of silver would be higher than it is today. This is an enormous amount of silver. People fret about the next million ounces in Silver Eagle sales or how much the ten million oz bought by Sprott would impact the market. That's because ten million ounces is just about all the new silver available each month, at the margin, for the world to invest in after all industrial fabrication is accounted for. Over the past 8 weeks, one entity sold short four times that amount. How can that not be manipulative to the price? I'm not making these numbers up; they are contained in the COT report and published by the same federal regulator, the CFTC, responsible for making sure something like this doesn't occur. The CFTC seems to be paralyzed by fear or reluctance to move against JPMorgan, but the question that won't go away is why would JPMorgan act so blatantly?

My guess is still that JPM thought that they had no choice but to sell such an outrageously large quantity of COMEX silver contacts. Otherwise, silver prices would have exploded. After all, the raptors sold what was expected that they would sell. If the big 4 hadn't sold almost 9,000 additional silver contracts short over the past 8 weeks, someone else would have to have sold in their place. This is not that complicated. JPMorgan was the seller of last resort because there was no one else to take their place. What is infuriating is that this appears only to be complicated to the regulators whose prime mission is to prevent or prosecute such an occurrence.

I've also had a chance to contemplate why it is that I have been able to say these things so openly and without objection. Certainly, I am no match for JPMorgan, as comparing an elephant and a flea doesn't come close to describing any potential mismatch. It occurs to me that in addition to intending no harm to JPMorgan, I am fulfilling a civic duty. I am reporting a crime in progress to the appropriate authorities. You don't get arrested by the police for reporting a crime being committed. Perhaps I am being naÃ¯ve, but that's as I see it.

I had an interesting experience this week. A fellow reader of these reports, who is also an old friend, was moved by my recent appeal (as were many of you) and took it on himself to arrange a conference call with me and his Congressional office. I must confess that after the call, I was somewhat disappointed as it was my read (as well as my friend's) that the staffer in charge was not really interested in prodding the CFTC about the stalled silver investigation. The staffer was seemingly making excuses for the CFTC (they were tied up with MF Global and rulemaking, etc) for why the silver investigation was taking so long. Quite frankly, I had low expectations and mentally wrote the effort off. Much to my (and my friend's) surprise, we each got a call from the staffer a couple of days later saying that he had spoken to the CFTC and confirmed that the silver investigation was drawn out, but was continuing. He also told me that the CFTC had indicated that a reason for the delay was that new information was being studied that wasn't available at the outset of the original investigation initiated in 2008. Perhaps I am reading too much into this, but hopefully, the new information includes the two manipulative 35% takedowns in price during 2011. If ever there was compelling new information to consider, it would be the rotten circumstances around those two deliberate declines.

If I appear unsure of the near term direction in price, that is not an act. As almost always is the case, we could go anywhere in the short term. Longer term, silver looks much higher. I am convinced, as I have been for more than 25 years, that silver is a crooked market and that is why I am pressing for a resolution by the CFTC in its silver investigation. I am less concerned with them saying (again) that there is no manipulation than I am with them saying nothing. Evaluating what has been openly put on the table is a lot easier to deal with than is debating silence. If you haven't contacted your representative or senator, please consider doing so. Nothing fancy, just point out that this is probably the longest running investigation in government history and that's plainly too long. Especially for a crime in progress.

Ted Butler

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Silver – $33.25

Gold – $1725

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