July 19, 2010 – More Good Questions

More Good Questions

Hi Ted,

I have 4 questions/concerns which I hope you will be able to address. The first three I assume you would likely be writing about in your next communication. They are as follows:

1- The meaning and timing of the new Sprott Silver ETF
2- The JP Morgan Chase London metals warehouse experiencing a theft. Is this a precursor to a similar silver incident that might explain a potential shortage?
3-The proximity of the current price of silver to 17.60. A fall below this price would break a meaningful trend line and likely trigger stops, which in turn could really provide some fuel for the silver shorts to push the price down much lower.

The last question/concern is more longer term in nature. Which silver users have benefitted and continue to benefit by the artificially low silver price. Is it possible they are complicit in what has happened or are they simply unwitting beneficiaries?

Good luck. I look forward to your comments.

Thank you.

Paul

I think the proposed new Sprott silver ETF is a great addition to the existing publicly-traded silver investment vehicles, especially when brought to market by such a well-regarded financial institution. I do take issue, however, with some reports that suggest this ETF will be the death-knoll for SLV, as I just don't see that. But the more legitimate silver investment vehicles are introduced, the better. (In the interest of full disclosure, let me say that Eric Sprott and John Embry are subscribers and I think the world of them).

No, the base metal warehouse thefts were an unrelated matter which actually occurred prior to JPMorgan buying the business. I don't see any connection with SLV.

To the contrary, I feel a fall below the $17.60 level (which has occurred as this is being written) should represent a clean-out of stale technical fund long positions below the 200-day moving average. I've mentioned this level in the last couple of King World News Interviews. While I look at charts closely, I look at them differently than most folks. Any time we are below all the important moving averages, like now, is a safer time to buy, as most, if not all of the liquidation is behind us. I admit that this is opposite of what most folks assume.

All the many tens of thousands of silver users worldwide have benefitted from the lower prices brought about by the silver manipulation, but that doesn't mean I think they are complicit in the manipulation. In the old days, I think the Silver Users Association played an important role in keeping silver prices depressed, but not in the last ten years or so, since the US Government ran out of silver. I do think, however, that the silver users will be hit hard once the manipulation is terminated, which I think is soon. I'll talk about this more in the future, as the silver users are critical factor number three.

Dear Ted

Firstly I want to thank you for coming on line with messages to subscribers on every occasion of a silver smack down, Those of us who are very long silver appreciate the view of an expert during these times.

I was reading a piece about the Hunt brothers recently, trying to relate what was happening to the silver market then as now, and it seems that tight physical conditions existed in similar respects, with a dominant player doing the naked shorting as today with JPM. So my question is why would the outcome of a short squeeze be any different this time? If the dominant players could not cover their positions legitimately, what would stop the regulator from changing the rules again to help them out? If I'm not mistaken, the position limits hurt the Hunt brothers too (why I can't figure) and even more so when liquidation bids only were imposed as the price of silver dropped after the introduction of this restriction and resulted in margin calls. If we assume that too big to fail will always be the regulators mantra, why should we not expect regulators to come to the rescue of a JP Morgan if market prices turned up abruptly against them, as you suggest will happen at some point?

Best regards
cos

While there are similarities in silver today with 1980, the differences are much more pronounced. Yes, there were concentrated shorts then (led by Mocatta), but the concentration is much more extreme today. Plus, we didn't know about the shorts until after the event was over, unlike today where we know JPMorgan's role in advance of any resolution.

The biggest differences have to do with the amount of silver in the world back then compared to what we have today. Thirty years ago, we had 2.5 billion more ounces in world inventories than we do today. Plus, the short position is larger and more concentrated today. This is an explosive combination. The silver problem today is so severe that there is no easy solution. That's a big reason why the regulators and JPMorgan are so silent in the face of public criticism.

It is true that the exchange and the big shorts and the regulators teamed up against the Hunts by changing the rules. It is also true that without the Hunts' big buying, silver never would have gone to $50 in the first place. We must be honest and conclude that the Hunts did manipulate the price of silver, rule changes or not. Contrast that to today. While many bemoan the fact that no one big has burst onto the silver buying scene, this is a blessing in disguise. Because there is no concentration on the long side, as there was in 1980, rule changes to force disgorgement on the long side would be ineffective. It's only manipulation if it is carried out by a few, not the many.

We can learn much about silver and manipulated markets by studying the Hunt silver episode. The real lesson lies in studying the differences. As my silver friend and mentor, Izzy Friedman, always reminds me Â? Â?if two Texans could push silver to $50 in 1980, what price could someone move it to today, with billions of ounces less in the world?Â?

I also received a good number of questions about my recent suggestion that this may be a good time to consider call options. I hope you realize that I'm trying to tread lightly in this area, while at the same time make a point. The main point is that the recent take down in price, including today, makes silver a better buy than it was before; not just because it's cheaper, but also because the market structure necessarily improves due to speculative long liquidation.

You know that I am not, nor do I wish to be a financial investment advisor. You also know that I constantly warn of the dangers of margin or leverage in silver. So where the heck do I get off hinting at the very speculative undertaking of purchasing call options? Everyone is captive to some extent to their background. My background was in commodity futures and options. At times when I perceive a near term bottom and a the potential of a significant price move up, I can't help but think of silver call options, even though they are considered high-risk. That doesn't mean you should. Studies have indicated that upwards of 90% of option buyers lose money. The record shows that the vast majority of cash physical silver buyers over the past 10 years are ahead. They will be much further ahead over the next ten years.

Since you must consider you will lose your entire investment in any one option play, you should never consider putting more than a very small percentage, say one percent or less, of your investment capital into buying call options. That’s how you control the risk, as you can't lose more than what you pay for a call option. The attraction is you do gain leveraged exposure to a big move while limiting your risk to what you pay for the option. You pay more for the longer the time period you choose and if you buy an option whose strike price is either in the money or at the current price of silver. If you buy short time period and Â?out of the moneyÂ? options, you decrease your chance for success. The shortest option time periods and the strike prices out of the money are the cheapest and hardest to profit from. Generally, those are the ones I am attracted to, because if you hit it right, these will be the most profitable.

Options are only for those willing to throw good money out the window, kind of like buying a boat. My advice is not to do it. But do as I say, not as I do. If you do decide to gamble on options, I'm concerned enough about the COMEX's future viability, that you shouldn't do COMEX options exclusively, but consider call options on SLV or silver mining stocks instead of or in addition to COMEX options.

Options aside, this recent smack down, as blatantly manipulative as it is, has created another great buying opportunity. Please handle it accordingly.

Ted Butler
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