

March 24, 2012 – Weekly Review

Weekly Review

After hitting new price lows on Thursday, gold and silver came back strongly on Friday. Gold's rally was enough to push it slightly higher (\$3) for the week, while silver still finished the week lower, off by 35 cents. As a result of gold's outperformance, the gold/silver ratio widened out to just over 51.5 to 1. While the market structure in each now indicates a bias towards higher gold and silver prices ahead, this would appear to me to be an opportune time to switch gold positions into silver. As always, no leverage advised.

The big news for the week was price action and the changes in the new Commitment of Traders Report (COT), but let me first run through the developments in the wholesale physical silver market. Turnover or movement in the COMEX silver warehouse inventories remained hot, with mostly net increases, as total inventories jumped towards the 136 million oz level. This is the highest level of total COMEX silver inventories in more than 3 years and up almost 30 million oz over the past few months. It would not surprise me if COMEX silver inventories continued to grow. I still maintain that an increase in COMEX silver inventories is not necessarily bearish for prices, but turnover is almost necessarily bullish. Despite the increase in COMEX inventories, the price of silver is still measurably higher over the same few months (including the past four week price swoon).

There has been some withdrawal of metal (1.1 million oz) from the big silver ETF, SLV, over the past week and that looks like plain-vanilla investor liquidation in response to the recent sloppy price action. All in all, changes in the holdings in SLV have been muted, first during the \$10 rise in silver since late Dec and on the subsequent \$5 decline. One clear conclusion is that the silver price moves had little to do with physical investment buying or selling and were all attributed to paper trading on the COMEX. Monday's release of the new SLV short position is awaited and my sense is that no big increase in that short position will be reported and, hopefully, further declines are in the offing.

Sales of Silver Eagles from the US Mint continue better than during the lull in February, but are not as blistering as they were for the whole of last year. Silver Eagle sales are still blistering compared to Gold Eagle sales, but overall retail demand is soft in each. I still maintain this has little bearing on short term silver price trends and I do expect retail demand to pick up as and when silver prices improve.

There was a dramatic further improvement in the market structures of both gold and silver in this week's COT report. Gold, in particular, witnessed a marked 25,500 contract net reduction in the total commercial net short position (even greater than my guess last week of a ten to twenty thousand contract reduction). This reduced the total commercial net short position to 166,100 contracts, the lowest since Jan 3. This week, it was the big 4 and the gold raptors doing the big buying; with the big 4 buying back over 15,000 short contracts and the raptors buying back more than 12,000 contracts, completely eliminating the raptors' net short position. (The big 5 thru 8 added a bit to their net short position). Interestingly, the big 4 in gold are now less net short than at any time since September 2007. That's another way of saying the four biggest gold shorts on the COMEX are now better positioned for a rally than at any time in four and a half years.

In silver, the commercial net short position was reduced by 3500 contracts, to 32,100 contracts, the lowest level since Jan 31. (Not quite the 5000 contracts or more that I was expecting). As in gold, it was the big 4 and the raptors doing most of the buying. The big 4 bought back 1300 shorts and the raptors added 2100 contracts to their net long position. My estimate for JPMorgan's net short position is around 21,000 contracts, still 25% of the total COMEX net open interest (less spreads). I'll comment further on JPM in a moment.

Let me summarize the current market structures in gold and silver before remarking on how we got here. The current gold structure is as bullish as it was back at the late December price lows, namely, very bullish. And please remember that there was a fairly high volume sell-off after the Tuesday COT cut-off in both gold and silver, meaning that the market structure is even more bullish than indicated in the new report. In silver, we are not back to the extreme COT readings of late December (as we are in gold), but those silver readings were so extreme that I doubt we can achieve them again. I suppose the commercials could rig lower prices ahead because you never want to say never. But any objective reading of the COTs now strongly favors the upside. As always, lower prices from here would only make the structure more bullish. That's where we are right now; how did we get here?

In broad terms, since late December we added roughly 80,000 net COMEX gold futures contracts to the speculative long and commercial short sides to Feb 28, the equivalent of 8 million gold ounces (worth over \$13 billion). This speculative COMEX buying caused prices to rise from under \$1550 to over \$1780. During this time and on the subsequent price decline over the past three weeks, there was almost no change in the physical holdings in the known gold ETFs, including GLD. On the gold price decline starting on Feb 29 through today, the same 80,000 speculative net long contracts were sold on the subsequent price decline to \$1630. In simple but accurate terms, gold first rallied \$230 on the purchase of 80,000 speculative COMEX contracts and then fell \$150 on the sale of those same 80,000 COMEX contracts. There were no other verified or documented significant gold transactions, paper or physical, that came close to the 8 million ounces of COMEX gold contracts over the past three months.

In silver, 30,000 net speculative contracts were bought on the ten dollar increase in silver prices from late December to Feb 28, the equivalent of 150 million oz. Since then, roughly 15,000 net speculative COMEX silver contracts were sold on the sell-off that commenced on Feb 29. Simply put, the net speculative purchase of 150 million oz of COMEX silver contracts first drove prices \$10 higher and the subsequent sale of 75 million oz of contracts then caused the price decline of \$5. These are enormous equivalent amounts of silver, the likes of which were not transacted in any other verified and documented market, paper or physical.

My point is one of cause and effect. Gold and silver rose because of speculative COMEX buying and fell because of speculative COMEX selling. Nothing else accounted for the price movements; not London or Asian trading, not any other paper or physical metal trading. Certainly, if anyone has any hard evidence of other significant trading, please send it to me. There were no big supply or demand developments in gold and silver over the past three months to account for the price changes; only what occurred on the COMEX. I'm not saying that fundamentals never matter, as they surely do, especially over the long term. I am saying that over the past three months, COMEX trading accounted for the price changes in gold and silver. I'm hard pressed to think of who might argue with that, given the evidence.

Undoubtedly, any other objective review you may read on the current COT structure will conclude that the price prospects for gold and silver are greatly improved as a result of the recent speculative net selling and commercial buying. It can hardly be any other way, even if we see further price erosion ahead. But likely missing from most of that other commentary will be how this improvement came about. It's one thing to note that the COMEX speculators first bought, then sold and by how many contracts. It's quite another thing to note how and why the speculators first bought and then sold. As you know, this has been the thrust of my recent message. While the speculators may not have been tricked into buying, they certainly were tricked into selling by the commercials.

I won't rehash the issue here, but it is not possible that the commercials could always be the buyers on all big selloffs, unless the game was rigged. The game is rigged and it is rigged by collusive commercial behavior, highlighted by price-rigging tricks like HFT. The only difference is that the regulators crack down on HFT when it involves unwanted moves in the stock market. When the crooked commercials employ HFT in COMEX silver or gold, the regulators look away.

If there is a special message I would like to convey today, it concerns the "flip-side." There is a flip side in everything; a yin and a yang, a good and a bad. In silver, the price manipulation is bad in that it is illegal and offensive to the rule of law. It's also pretty good in that it has and does enable investors to buy an undervalued asset. One of flip sides I have been thinking about lately concerns JPMorgan, the CME Group and the CFTC. It came to me after a recent phone conversation with an attorney who had considered going after the silver manipulators.

The lawyer had called me, after hearing from a reader and looking at the issue. He was qualified, in that he practiced litigating against big banks and companies for financial fraud type offenses and had just come off a big win (\$100 million), which included JPMorgan on the other side. He decided against pursuing the silver manipulation case, not on the actual merits, but on the financial costs and risks to the law firm. Going after a JPM or CME on a case of market manipulation is financially akin to a multi-year siege of a city-state during the Middle Ages. It's not an undertaking assumed lightly, so the lawyer took a pass.

There is no question that JPMorgan and the CME Group are near-invincible to legal attack, perhaps even by the US Government. The CFTC, in turn, is part of the US Government and appears also beyond attack (except by Congress). All three entities are ignoring the silver (and gold) manipulation with all their might, even though it is smack dab in front of them and important beyond words. Admittedly, this is frustrating and difficult to contend with and there appears little additional we can do about it. But like in everything else, there is a flip side here as well.

The flip side to JPMorgan and the CME Group and the CFTC is that their collective silence in response to allegations of manipulation is that it does nothing to rectify the situation; it only postpones the day of reckoning. In the interim, their reputations are further tarnished and potential liability grows. The longer the manipulation continues the more potential risk to the perpetrators and the regulators. One of the strongest confirmations of the silver manipulation's existence is the continued existence of the concentrated short position of JPMorgan.

Putting myself in JPM's shoes, I would have done everything possible over the past 4 years to get rid of this big silver short position. If JPM had closed out the big short position that would have made the allegations of manipulation disappear. They would have been home free. Instead, the allegations of manipulation are stronger than ever, including reputational harm and greater potential risk. Same for the CME and CFTC. It looks to me that the flip side is that the big short position can't be closed out quietly and that while appearing invincible, JPMorgan is also stuck between a rock and a hard place. That's why they sold additional short contracts in the price rally to Feb 28; they had no choice.

Now JPMorgan is short 21,000 silver contracts (maybe 20,000 since after the cut-off) and the COT set up looks for higher silver and gold prices. That arguably the most important financial institution in the US is short that or any amount of silver is bizarre. Yeah, I know they are invincible, but there is a flip side to invincible as well. I know JPMorgan doesn't want to be short silver as it only detracts and does not add to their franchise's value and reputation. I just don't know what they can do about it. JPM might not know either. But whatever they do, it will impact the price of silver. Of course, it shouldn't be that way.

The COT structure is now great in gold and silver. It feels like we have seen the lows, but that is less important than being close to the lows. JPM's short position is still the wild card, but I suppose there always has to be a wild card of some type.

Ted Butler

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Silver -\$32.25

Gold – \$1663

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