

## March 31, 2012 – Weekly Review/Is JPM Stupid?

### Weekly Review

After a strong start and then a sell-off midweek, the price of gold and silver finished mostly flat for the week. Gold managed to add \$5, while silver was unchanged. The gold/silver ratio was up a bit, but still below 52 to 1. All the signs I monitor continue to point to silver outperforming gold over the long run. The chief sign is still relative dollar valuations, with my premise mostly centered on it being easier for a smaller market to rise faster and farther than a larger one. World gold bullion inventories are measured in dollar terms in the trillions, while silver bullion inventories are valued in the low tens of billions of dollars.

Of course, long term valuations are rarely involved in daily and weekly price changes. For short term movements we look to other factors. The trick for long term investors is to look at the shorter term factors through the filter of the long term. Admittedly, this is easier said than done most of the time.

Conditions in the wholesale physical silver market continue to suggest tightness, according to my principle indicator of COMEX warehouse turnover. COMEX silver warehouse inventory movement certainly continued frantic this week, as total inventory levels slightly exceeded 137 million oz. It is now more than a year since the heavy movement of COMEX silver inventories first appeared and I admit to still being awe-struck by this phenomenon. And I still can't come up with a more plausible explanation for the turnover than supply tightness and a hand to mouth mentality in some quarters of the silver supply and distribution chain.

There was some minor movement in the holdings in the big silver ETF, SLV, for the week, but my main takeaway there is that relatively little liquidation took place on the recent \$5 pullback from the \$37 price high of Feb 28. Coupled with the recent sharp decline in the short position of SLV (hooray!), it looks like the vast majority of shareholders are settled in for the long term. This appears true in other silver and gold ETFs as well. I can't help but interject that physical investment holdings in gold and silver have little to do with short term price movements; almost all short term price change can be traced to paper COMEX dealings. This is a classic case of the tail wagging the dog. It appears that the regulators at the CFTC have reconciled themselves to ignoring the spirit of commodity law.

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Sales of Silver Eagles finished the month up from the very disappointing levels of February, but were still not particularly impressive; same for Gold Eagle sales. Of course, going back further than the past few years, current sales of Silver Eagles still look impressive; but it's always a case of what have you done for me lately? I'm still convinced that retail silver demand will soar as prices resume an upward trajectory, but the timing is always unknowable.

[http://www.usmint.gov/mint\\_programs/american\\_eagles/?action=sales&year=2012](http://www.usmint.gov/mint_programs/american_eagles/?action=sales&year=2012)

The changes in this week's Commitment of Traders Report (COT) were somewhat surprising at first blush due to a sharp divergence between gold and silver; but much less so after studying all the data. The total commercial net short position in gold grew by almost 19,000 contracts, while in silver the total commercial net short position fell by a relatively hefty 2400 contracts. Let me explain why I think the divergence occurred before getting into the specifics of the changes.

To appreciate the divergence, you must look at the situation through the eyes of a technical fund or trader, especially those motivated by moving averages. During the reporting week, there was a large gain in gold and silver prices on Monday and into early Tuesday on fairly high trading volume, particularly in gold. Most importantly, certain moving averages, including the 200 day and 20 day moving averages in gold were penetrated to the upside. Given gold's oversold condition and bullish COT structure, the penetration of these moving averages in gold resulted in strong technical buying and the reciprocal commercial increase in short selling. In silver, although there was also a strong rally on Monday, the silver moving averages were never penetrated and no big technical buying occurred. In a nutshell, that's why gold deteriorated and silver improved. Of course, there was a sharp sell-off on Wednesday, after the cut-off, and both the gold and silver structure likely improved on that sell-off.

In gold, it was the big 4 and the raptors (the smaller commercials apart from the big 8) doing most of the selling, with the big 5 thru 8 traders adding almost 1200 contracts. The big 4 sold more than 9000 contracts short and the raptors a bit less than that. Still, according to a quick glance at my scribbled notes, the big 4 are holding their second smallest net short position in more than four and a half years, back to when gold traded close to \$700 an ounce. Therefore, the biggest gold shorts are still positioned for a rally. Despite the big weekly increase in the commercial net short position, at 185,000 contracts, the total short position is still at bullish readings. And, if I had to guess, I would think at least half of the weekly increase in the commercial short position was bought back on Wednesday. Gold is still structured to go higher, rather than lower.

In silver, the entire 2400 contract decrease in the total commercial net short position (now at 29,700 contracts) can be attributed to the big 4 (read JPMorgan). Accordingly, I would now calculate JPMorgan's concentrated silver short position as being roughly 19,000 contracts. This puts JPM's silver short position about midway between the 13,000 contract low point of late December and the recent 24,000 contract high-water mark of late February. Minus all spreads, this means that JPM is holding 23% of the entire COMEX futures open interest. It is not possible for that percentage of concentration not to be manipulative to the price of silver. I'll speak separately of JPMorgan in a moment.

The bottom line is that the COT structures in gold and silver are still favorable. Can the commercials still collusively rig prices lower? Of course, they can, but that will only make the set up better. In COT terms, there is much more price room to the upside versus the downside. An added takeaway is the hint of a possible very sharp rally given how quick and forceful some technical traders entered the long side of the gold market on Monday's rally. I would look at that as a harbinger of what may come, namely, strong technical type buying once the moving averages are penetrated to the upside in gold and silver. At that point, it will become a question of how aggressively and manipulatively the commercials will be selling. Just make no mistake – this paper trading on the COMEX is the sole determinant of short term price movement. This is price setting, pure and simple. This is also about as far removed from the price discovery function of futures markets intended under commodity law as can be imagined.

### Is JPMorgan Stupid?

Analysis is the attempt to take all the known facts about a topic and weave, separate and prioritize those facts into a logical premise or course of action. At least, that's what I try to do in silver. To analyze properly, you need core beliefs but must remain open to all possibilities. As a result of a contact by a long time reader, it occurred to me that I may not have considered all the possibilities for explaining the critical element behind the silver manipulation, namely, why does JPMorgan continue to hold such a large concentrated short position in COMEX silver futures?

This is a separate consideration from whether JPMorgan holds a large concentrated short position in COMEX silver, as that is easy to establish from data and correspondence from the CFTC. We're now talking why do they continue to hold this position? I still believe it is much more important that the position exists (as I hope I've previously written) than why it exists, but reasoning why JPM would hold the silver short position is of no little concern. Up until the recent contact by the reader, I had it narrowed down to either JPM was merely an arm of the US Government intent on capping gold and silver prices (the most popular explanation) or it was JPM on its own with the CFTC too timid to take them on (my guess). My point is that I thought it was narrowed down to either of those explanations. The reader's contact opened up another possibility.

Certainly, the reader didn't ask if JPMorgan was stupid in any way or in any words close to that. I don't recall him even mentioning JPMorgan, although he may have referred to big silver shorts in general. He rather made the point that all the facts pointed to silver being an asset that should go a lot higher in price, so why would anyone want to be short it in extremely large quantities? There was nothing insulting in his words; it was more a matter of incomprehension. Who in their right mind would want to be heavily short silver to the point of manipulating it? Likewise, I'm not trying to insult JPMorgan because at this point that would seem to be secondary to my more serious allegations of manipulation. As I said at the outset, analysis involves considering all the possibilities and a new one suddenly crossed my mind. Perhaps stupidity is too harsh of a word and ignorance would be softer. Maybe JPMorgan just doesn't really know what it is doing in being short silver.

Just to be clear, I still believe JPMorgan is smart beyond description and it knows full-well the ramifications of its giant COMEX short position. I don't think JPM necessarily knew all the ramifications of the silver short position when it took it over from Bear Stearns four years ago; but it is too well-connected not to have grasped it by now. Among the attention-getting road signs along the way, I would imagine having some 30-odd class-action lawsuits filed against you for manipulating silver might force you to become aware of your position. I'll leave out the hundreds of my articles that I sent to JPM, but I would include the 3.5 year CFTC silver investigation as another attention getter for JPMorgan. The CFTC never talked to me, but I would hope to the heavens that they at least spoke with JPM. Then again, who really knows? And if the CFTC never knocked on JPMorgan's door concerning the silver manipulation and their concentration on the short side that would actually boost the JPMorgan doesn't fully know possibility.

I looked up the word stupid in the dictionary and the first few meanings included acting in an unintelligent and careless manner and being obtuse. Throw in arrogant (easy for me to imagine) and stupid doesn't sound so stupid for why JPMorgan would stay short silver. Remaining deliberately oblivious to a circumstance that holds potentially grave consequences might also be considered a natural defense mechanism. Maybe it's a combination of things, like being stuck in a position and not wanting to fess up to it. So JPMorgan just pretends nothing is amiss. But that doesn't sound like a good long term strategy for dealing with a serious problem. The stakes are so great in silver being manipulated that, sooner or later, it will be discussed openly by someone like the CFTC, JPMorgan and the CME Group. Currently all three are engaged in a game of silver mum's the word, even though a supposed official investigation is ongoing and class-action lawsuits are pending.

Here's another possibility Â? perhaps it is me who is being stupid. Maybe I'm just imagining this blatant manipulation. Perhaps JPMorgan doesn't hold an unusually large concentrated short position. Maybe it's not collusion that explains how the commercials all buy as one after they smash prices down. Maybe there's a legitimate explanation for all the questions that arise in silver. But if there are legitimate answers, then why aren't those answers being offered forthwith? Where's the good to JPMorgan, the CFTC or the CME by them keeping silent? Certainly, the respective heads of these organizations command prime air-time whenever they desire. It's about time for all of them to set the record straight and openly address claims of wrongdoing. Let's find out who's being stupid.

Unless I'm completely misinterpreting it, Chairman Gary Gensler of the CFTC has opened up a new front against the big banks in derivatives regulatory reform. In three important speeches in as many days, Gensler has hit upon a new note. First, let me not disguise my profound disappointment in the chairman for how he has neglected the ongoing silver crime in progress. To whom much is given, much is expected. Gensler has been given all that is necessary to crack down on the silver manipulators and he has failed to do so. Be that as it may, his failure does not become our failure unless we allow it. Perhaps he will redeem himself in silver in time. Remarkably, away from silver, Gensler truly is fighting the good fight. On my report card, he gets mostly all A's, with one F for silver. (I wouldn't even give him an F for MF Global, because if we are grading on a curve, no one can get a lower grade than the CME). Interestingly, the first of Gensler's speeches this week was to the US Chamber of Commerce and in response the Chamber's report card on financial regulatory reform.

<http://www.cftc.gov/PressRoom/SpeechesTestimony/opagensler-110>

The important new point that Gensler is raising is the overwhelming dominance by financial firms of the entire commodity swaps and futures marketplace. The real non-financial commodity producers and merchants account for as little as 10% of the swaps and futures markets, with financial firms holding 70% to 90% of the market. In other words, the share of derivatives (OTC and listed futures) held by real commodity producers and consumers is tiny and prices are dictated by purely financial firms, namely big banks. This is something I have thought about often. Few silver mining companies appear to hedge their silver production. In fact, many have taken a public pledge to shareholders never to hedge silver. Then what about all the stories about the banks holding legitimate swaps with producers? In reality, the big silver concentrated short position is a paper scam between banks pretending to be hedging and other speculators. Please read the chairman's speech and see if you don't come to the same conclusion. As always, I am hopeful that Gensler will reflect on his own words when it comes to silver.

In the remarkable coincidence department, Commissioner Bart Chilton gave a short speech this week at the opening of the agency's first meeting of its Technology Advisory Committee, mostly a group from the High Frequency Trading (HFT) world. Chilton's speech was titled "Day Tripper" and was patterned after the famous song by the Beatles.

<http://www.cftc.gov/PressRoom/SpeechesTestimony/chiltonstatement032912>

The coincidence is that I wrote an article with the same title, based upon the same song and concerning the same HFT issue last June 29 (in the archives). My conclusion, then and now, is that HFT provides no economic benefit to real producers and consumers who come to the market to hedge. How can frantic day trading, no matter how large, help a legitimate hedger interested in locking in long-term price protection? Since HFT day trading provides no such benefit to legitimate hedgers, it should not be allowed at all, in my opinion, especially when it is used extensively to further the silver manipulation. Commissioner Chilton doesn't go that far, but compared to his past comments about HFT, his current take is closer to mine than it used to be. As always, you decide.

It's really quite simple. Modern futures and swaps markets have nothing to do with the spirit and intent of why congress allowed organized futures trading in the first place. The economic purpose behind futures trading rests upon affording legitimate producers and consumers the opportunity to lay off price risk to speculators willing to assume that risk. Instead, the futures markets have evolved into a circus where big banks and other speculators game the system by day trading with super fast computers and control prices with no relation or benefit to legitimate producers and consumers and underlying real supply/demand fundamentals.

Think I'm overstating it? Consider this  $\hat{A}$ ? just at a time when many market participants have come to realize the harm that HFT practitioners are doing to our markets, what does the primary regulator do about it? The CFTC holds a hootenanny and invites the leading practitioners to Washington to hear their views. All this, while the agency ignores the clear evidence and many thousands of complaints that these same computer jockeys are manipulating prices. I couldn't make this up if I tried.

The important point here is that both Gensler and Chilton seem to be awakening to things that silver investors already knew to be painfully true. The big banks and computer mad men have taken control of pricing from legitimate producers and consumers (including investors). This is an outrage that cannot be allowed to stand. The speeches are encouraging, but the time for only talk has long passed. JPMorgan and the CME Group are manipulating silver and other commodity prices. Who cares if they are being stupid; they are doing something illegal. If the commissioners can't see this and do something about it, it is time to replace them with those who can.

Ted Butler

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Silver – \$32.25

Gold – \$1668

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