September 9, 2010 – Comments and Q&A

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Silver has been churning around the $20 mark since my last update. My feeling is that we won't be churning at this level for too long. I wish I could assure you of the very near term price direction, but I am convinced no one can. The long term is more certain and that direction is up. Silver should explode in price, but that is something that should have occurred long before now (notwithstanding silver's multi-fold increase in price over the past 5 to 10 years).

I'm encouraged by recent widespread bullish commentary on silver's near term price prospects, but also unnerved a bit when everyone is saying the same thing. To me, the next short term move in silver will be determined, as it always is, by the interplay between the tech funds and the commercials on the COMEX. If we drop sharply, it will only be due to the collusive actions of the big commercial shorts and other traders on the COMEX. That this set up is still what determines price moves is disgraceful. It is manipulation at its worst. On the other hand, it is always possible for the crooked shorts to get run over, given all the bullish forces at work in silver. Near term nervousness aside, it is important not to be out of position for the major up move to come in silver. Quite frankly, I don't think I'd be surprised by whatever the near term price action might be. We must be prepared for anything and to not lose long term silver positions.

The new COT and Bank Participation Reports are anxiously awaited, as they will provide strong evidence as to what JPMorgan and the other big silver shorts have been up to. I plan on reporting the details in Saturday's Weekly Review. In the interim, I continue to get good questions from subscribers and I'd like to share a few now. If you've asked a question, but have not received a response, please ask again.

Ted,

Thanks for such prompt and informative answers to my last questions. Another question for you. In reading up on silver it is often quoted that there is less silver above ground than gold – an astonishing fact when heard for the first time. Further it is stated that there is about 500M-1BN ounces of silver bullion bars in existence. By that I assume they mean 1,000oz bars in secure vaults. However sometimes it is stated that there is a substantial amount of silver in “private hands” – not bullion stored in vaults just private silver. By this I guess what is referred to be silver jewellery, silverware, flatware etc.

How much of such silver is there? Also going back to silver bullion where on the 500M-1BN scale do you think the true amount is?

Please feel free to answer publicly and in your own time, this is not urgent but this does puzzle me.

Regards, Edmund

Edmund.

Since this has been one of my main observations, thanks for the opportunity to address it. Over the span of history, roughly 5 billion ounces of gold and 40 billion ounces of silver have been taken from the earth. Therefore, on any measurement of how much exists of either metal in every form possible, there is more silver than gold, given their cumulative productions. However, a slightly deeper analysis readily reveals that in spite of there being greater amounts of silver in the Â?all formsÂ? category, in the all important bullion in existence category, there is actually more gold than silver.

That's due to many factors, including gold's always higher price and silver's widespread industrial applications. Gold's rarity and higher price have prevented it from being widely used industrially, resulting in it being preserved as a store of value and being readily available for melt. Conversely, silver's relative low price and historical abundance has resulted in widespread dispersion and it not being readily available for melt at current prices. My guess is that of the 5 billion ounces of gold produced and said to exist above ground, 2 to 3 billion ounces is in bullion form. Of silver's 40 billion ounce cumulative production, I think one billion ounces exists in bullion form. Incredibly few of the world's investors know this.

The key question is what price it would take to draw out the potential billions of ounces of silver from the all forms category to be converted into bullion when and if there is not enough silver bullion to satisfy industrial and investment demand. No one knows that price, but clearly, we haven't seen it yet, due to no noticeable surge in silver melt to date. Therefore, it would appear, from a potential silver melt to come perspective that the high price is still ahead of us. The great thing about any silver melt, should it come, is that it will be readily observable, as it was in 1980. As silver investors and analysts, we will observe and deal with it when it comes.

Dear Mr. Butler

I’ve two questions regarding how the CFTC does allow exemptions to position limits in the silver market (i.e. how the CFTC guarantees the “bona fide hedger” status to a trader).

Maybe you can help me. I’m a member of an internet forum on precious metals and I posed these questions over there too, but nobody can answer them.

I’ve read that the criteria for exemption looks only to a trader's CLAIMED inventory for qualification as bona fide hedger.
I don’t believe that in order to enjoy exemptions to position limits traders have only to CLAIM to possess silver inventories.
On the other side, for sure CFTC staff members don’t go and check by themselves.

Thus my first question: how does the CFTC’s check works in regard of claimed silver inventories of bone fide hedgers?

I’ve read also that the Commission allows the MERE POSSESSION of (or DIRECT CONTROL of) physical metal inventory as a qualifying criteria for hedgers seeking exemptions to position limits.

Mere possession, direct control … the CFTC doesn’t seem to require OWNERSHIP.

Now, JP Morgan is the custodian of a silver Exchange-traded fund, namely the SLV.
Thus my second question: can we say that the custodian of the SLV inventory has a “mere possession” or “direct control” of the silver bullions? I.e. is JP Morgan availing itself of its position as custodian of SLV inventory in order to enjoy position limits exemptions in the futures silver market?

Thanks in advance
Marco

Marco,

Up until now, the exchange is responsible for verifying the legitimacy behind any exemption granted from position limits for bona fide hedging purposes, with the CFTC in a general and distant oversight role. In the case of silver, the COMEX (part of the CME Group, Inc) is supposed to be the policeman. That's as crazy as it is letting the exchange set position limits in the first place, because of strong conflicts of interest. No exchange is interested in preventing traders from trading, because that is how the exchanges make money. The big traders seeking exemptions from position limits are invariably important members of the exchange itself, so basically it's all on the honor (or dishonor) system. There is no full disclosure. The new law promises to change that, by having the CFTC set and review exemptions. The way it has been done has been a travesty; but going forward I'm real encouraged.

What determines a bona fide hedge exemption should be based upon actual annual production or consumption or on actual ownership of the commodity. There is no reason not to disclose the particulars behind any exemption and it is my understanding that the CFTC is proposing to make the process more transparent. This is all good stuff.

As far as JPMorgan using its role as custodian of the SLV as some type of justification for holding a big short COMEX position, that doesn't carry water. The silver ion the SLV doesn't belong to JPMorgan, it is owned, effectively, by the shareholders. Whatever excuse JPMorgan can come up with to explain their big COMEX short position, it shouldn't be holdings in the SLV.

Ted,

I understand that the COMEX is the most important metals market, but could you comment on trends in other markets like London, Hong Kong, etc.
Also, comment on foreign ETFs please.
Thank you,

John

John,

It's hard for me to comment on these other markets as so little verifiable information is available. Even the LBMA's monthly reported volumes are unsubstantiated. We're all really quite fortunate to have so much verifiable data available from the CFTC involving COMEX trading. Also, have you ever noticed when we have a unique US holiday which closes COMEX trading, but not foreign trading, how there is hardly any trading anywhere? This past Monday (Labor Day) is a prime example. Someday, foreign trading of silver may be important, but not up until now. Besides, if you look at the big members of the LBMA, they are the same as the big members of the COMEX.

As far as foreign ETFs, I like the big silver ETF from Switzerland, ZKB, as well as the one from Julius Baer.

Hello Ted,

In one of your weaker moments you may or may not want to answer this.
Thinking outside of the popcorn popping pan, with much less silver bullion available for investment than gold what ratio could be seen between the two?
Kind regard, Gary

Gary,

I think it is better to think of the potential circumstances and forces that may come into play, rather than trying to pick a price target on the gold/silver ratio. This goes along with my suggestion to think of when to sell silver based upon changing facts, rather than an arbitrary price. For instance, if we see a genuine COMEX silver short-covering, and/or a true investment rush into silver, and/or a silver industrial user buying panic, the price of silver will move disproportionately to the price of gold. After all, gold has already had a bit of an investment rush and shouldn't experience an industrial user panic. When all those things play out in silver, it should be fully valued in the gold/silver ratio and silver may no longer be undervalued relative to gold. In number terms, it's hard for me to see how that could occur at anything more than a ten to one ratio. Some, including my silver mentor Izzy see silver being priced the same or more than gold, but even a 10 to 1 ratio would mean silver will ultimately outperform gold by five or six times from here. That's why I suggest gold investors switch to silver.

Dear Mr. Butler
I love your work even though it makes me aware of how much I don’t know. My question today involves the large short position in silver. I can understand why the accumulation phase of this large short position would undermine price because it involves active selling but I don’t understand why, after the selling is over and the large short position has been accumulated, the price is still affected. Would you please try to explain?
Thank you for all of your hard work.
Milo

Milo,

You are correct that the price-capping impact of the short sale is made at the time of the sale. You are also correct in that, over time, the price has risen in spite of these short sales. But the price would have climbed a lot more had these short sales not occurred at all. This is the key question to ask about whether a position is manipulative or not Â? what would the price be without the position? Remember, I'm not asking what the price would be if many traders didn't buy or sell, I'm asking what the price would have been if one, or just a few traders didn't buy or sell? This is what the regulators always look for in any manipulation case Â? what impact did one or a few traders have on the market? And was their position economically justified or were they just trying to influence the price to their unfair advantage.

The other aspect to the influence of the concentrated short position is that it is an open position, meaning it must be closed at some point, either delivered against or bought back. Because the big commercials shorts have so much to lose should the price of silver climb, they are motivated to resort to dirty tricks to close out their positions. That's where we stand right now Â? the market is at risk that the commercials will collusively rig prices lower to induce technical fund selling. That's not to say they will be successful, just that the market itself is diminished by their manipulative schemes. It is an outrage that they are allowed to exert such a dangerous control on the silver market. The big commercials have created a danger of a sell-off and a danger of a disorderly price explosion. They shouldn't be allowed to create such a dual danger.

Ted Butler

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Silver – $19.85

Gold – $1249

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