

## August 29, 2015 – Weekly Review/Freeport

### Weekly Review

Gold prices fell after two up weeks, ending the week lower by \$26 (2.2%), while silver wiped out four weeks of gains by falling 70 cents (4.6%) and establishing new six year price lows. As a result of silver's distinct relative underperformance, the silver/gold price ratio widened nearly 2 full points to just under 78 to 1, after trading near 80 to 1. This is the most undervalued silver has been relative to gold in nearly seven years. If you are a proponent (as I am) of investing in undervalued assets, this is the best time in 7 years to switch from gold to silver.

There are some similarities in silver today as there were in late 2008, when the price ratio to gold widened to nearly 85 to 1. Back then, it was the price of silver falling much further than gold that accounted for extraordinarily wide price ratio, same as today. Then and now silver hit multi-year price lows. Also as was the case both then and now, the depressed price of silver set off shortages and growing premiums on retail forms of silver.

Most similar is the cause of the big fall in silver prices then and now – futures contract positioning on the COMEX. More specifically, the big silver kingfish has remained the same, JPMorgan. Some differences would include JPMorgan now owning massive stockpiles of physical silver where it didn't seven years ago. What remains to be seen is how the silver/gold price ratio plays out over time. Back in late 2008 the ratio tightened in from nearly 85 to 1, to nearly 30 to 1, a little more than two years later as silver outperformed gold by hundreds of percent. Can or will that happen again? I think so, based upon all the facts.

That silver or gold would be down in price at all in current circumstances is a bit unbelievable in that there is nothing in the real world of metals to begin to explain the price action. Given stock market volatility and concrete evidence of strong real metal demand, the fundamentals have been tossed aside. And it's not just gold and silver, as other metals (copper, platinum and palladium) and other commodities, like crude oil are gyrating wildly with nary a hint of any change in actual production or consumption. The great tail of COMEX/NYMEX price setting is roiling and wagging the world of real commodities like never before. I'll come back to this theme later.

Turnover or the physical movement of metal brought into or taken out from the COMEX-approved silver warehouses maintained the 3.7 million oz movement of the prior week, as total inventories rose by 0.8 million oz to 171.2 million oz, following weeks of reductions. I would have expected more of an increase this week given the start of a traditional COMEX silver delivery month, but these things are hard to handicap. I should note that earlier in the week, JPMorgan did bring another 600,000 oz of metal into its own warehouse, leaving 2.5 to 3 million oz yet to go according to my silver racing form.

There are other factors on the COMEX to talk about, but it still amazes me how so few acknowledge the unprecedented physical movement of silver in the COMEX warehouses, as this movement stands out like a sore thumb as an indicator of wholesale tightness. Delivery intentions for first notice day on the September silver contract were announced and indicate a light number of 167 deliveries being issued and close to 2000 contracts or so still open.

While that number of contracts still open is not large by historical standards, it was hard to ignore the pronounced tightening in the spread differentials between the now spot month of September and the now lead trading month of December in COMEX silver. Over the last three days, the September to December spread differential tightened by 2.7 cents to end at only 1.5 cents at yesterday's settlement. To my mind, this is one of the tightest spreads I can remember on a first notice day.

I don't want to confuse anyone with esoteric details which matter little in the end. While this may be a fleeting indicator, what can be said about the tightening is that there was pronounced aggression on the part of those wishing to buy the September contract on a spread basis with December. Since this has occurred as September has become active for actual delivery of silver, it can be concluded that more were either interested in taking delivery of silver or not having to make physical delivery. In either case, it's considered a sign of potential physical tightness. By itself, it may not matter much, but taken with all the other signs of tightness in silver, it makes this old spread trader sit up and take notice.

I also noticed that JPMorgan showed up as a stopper (taker) of 29 silver deliveries in its house or proprietary trading account, the same as it has done in the previous traditional COMEX silver delivery months this year (March, May and July). While that is admittedly a small number of contracts, JPM was the second largest stopper on first notice day (after ScotiaMocatta) and that suggests it will stand for more silver contracts as they are delivered based upon the COMEX's formula for how deliveries are apportioned. Apparently, JPMorgan is not finished accumulating actual silver (which may account for why prices are so weak).

[http://www.cmegroup.com/delivery\\_reports/MetalsIssuesAndStopsYTDReport.pdf](http://www.cmegroup.com/delivery_reports/MetalsIssuesAndStopsYTDReport.pdf)

Switching to COMEX gold deliveries, the standout pattern in the just concluded August delivery period established earlier in the month, held true until the last day. The pattern featured Goldman Sachs as the biggest stopper (taker) of actual gold deliveries, all in its house or proprietary trading account. Goldman ended up taking an even 2500 gold deliveries (250,000 oz) of the total 5113 issued. Another feature was that the big gold issuer for the month was JPMorgan in its house account. But JPM issued all its house account gold deliveries (2750 contracts) very early in the month and did not issue more since then (although some of its customers issued deliveries as the month wore on).

Goldman Sachs had to wait until the last three delivery days to get all the August gold deliveries it was standing for, confirming indications earlier in the month that there were big stoppers waiting on the metal to be delivered to them, which is very suggestive of tightness in gold. Also suggestive of tightness is that such a quantity of metal (250,000 oz) was even arranged on a COMEX futures contract instead of more anonymously via a private bank to bank transaction. COMEX deliveries, particularly those done in a clearing firm's house or proprietary trading account, are among the most transparent of commodity transactions. So, for Goldman to take actual possession of close to \$300 million worth of gold makes you ask why they left such an easy trail to follow? One possible answer is that it was easier and cheaper to take delivery via COMEX futures contracts because other sources were unavailable. If so, that would underscore the sense of tightness in gold.

But at the same time Goldman Sachs was taking more gold than anyone else in the August contract, its chief commodities analyst/spokesman, Jeff Currie, was on CNBC badmouthing gold's price prospects. Talk about a mixed message and potential conflict of interest — have your public mouthpiece talk down gold while the firm itself is taking delivery of more gold than any other entity on the COMEX for the month. At the very least, Goldman shot itself in the foot for not recognizing how easy it was to track what they were taking delivery of and how that conflicts with the public statements made.

Sticking with gold, metal still seems to be flowing into the big gold ETF, GLD, also in keeping with the premise of tightness. There were also close to one million oz added to the big silver ETF, SLV, yesterday and we never did see any liquidation based upon the weak silver price action, as I had expected. In addition, there seems to be unusually strong demand for Gold Eagles from the US Mint along with the usual strong demand for Silver Eagles.

There is one more reporting day left for August (on Monday), but sales of Gold Eagles through yesterday indicate that over the past three months, monthly sales of Gold Eagles have spiked by nearly four times over the monthly rate of the four prior months. I continue to believe that the sudden surge in demand for Gold Eagles may have depleted Mint inventories of Gold Eagles in the same manner that inventories of Silver Eagles have been kept near depletion over the past 4.5 years.

[http://www.usmint.gov/about\\_the\\_mint/index.cfm?action=PreciousMetals&type=bullion](http://www.usmint.gov/about_the_mint/index.cfm?action=PreciousMetals&type=bullion)

And I sense that there is a common connection between the surge in sales in Gold Eagles as there was (up until recently) in sales of Silver Eagles, namely, the presence of a big buyer. But whereas the big buyer in Silver Eagles looked to be JPMorgan, I'm less sure who the big buyer is in Gold Eagles, although it could easily be JPMorgan there as well. Gold and Silver Eagles are most often thought of as purely retail forms of metal and the program was started 29 years ago to provide an adequate supply of coins to retail collectors and investors. However, nothing precludes a big buyer from amassing a large quantity of coins over time and that is just what I believe JPMorgan has done in Silver Eagles.

There is a difference currently between Gold and Silver Eagles. While the Mint may have depleted its inventory of each thanks to a big buyer, the lack of Silver Eagles has resulted in a retail rush for all forms of silver, with exploding premiums and delivery delays expanding by the day. Quite frankly, we are suddenly in one of the tightest markets for retail silver in years, quite comparable to late 2008 (as indicated above).

If an intelligent form of life were to appear from Mars, armed with the knowledge of how the law of supply and demand was supposed to work and observed silver prices at multi-year lows accompanied by surging demand for retail silver that threatened to cross the firebreak into the wholesale market (given all the signs of tightness), I would imagine the visitor would be at a loss to compute how this could be. If the visitor was intelligent enough and it was explained how the COMEX sets prices, I would imagine the visitor would be confused no longer, but would instead be amazed that the regulators did nothing about these circumstances.

The changes in this week's Commitments of Traders (COT) Report were fairly close to my published expectations, when viewed through the prism that such guesses are more akin to the accuracy associated with tossing horseshoes or hand grenades, rather than the surgical precision of a laser. I was off by a good number of contracts in gold, but at least got the direction and general magnitude correct and was closer in silver.

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You'll remember that gold prices surged through the 50 day moving average for the first time in months on high volume during the reporting week, while silver prices struggled. It was clear that managed money technical fund buying and commercial selling occurred in gold, with the only question being how much.

In COMEX gold futures, the total commercial net short position expanded by 32,700 contracts to 62,600 contracts. (I had guessed an increase of 50,000 contracts or more). This is the largest commercial net short position since June 30 and the largest weekly increase since May 19. By commercial category, the big 4 shorts added 10,000 new shorts and the raptors (the smaller traders apart from the big 8) sold more than 27,000 long contracts, leaving the big 5 thru 8 as buyers of 5000 shorts (a managed money trader or two may have been in this category).

On the buy side in gold, while there were some changes in the other reportable and non-reportable trader categories which canceled each other out, the managed money traders bought nearly the exact same number of contracts (32,700) that the commercials sold. This underscores that the two big categories are the commercials and the managed money traders in almost every market. Managed money traders added 7381 new longs and bought back 25,316 short contracts. I hate to see so many technical fund shorts bought back during one reporting week, but gold did rally more than \$50 at times during the reporting week and if there is a more compelling reason for the rally, I'm not aware of it.

I'm glad to have overstated what I thought the commercials had sold and the managed money traders had bought, since it puts the gold market structure in a neutral, rather than bearish mode as I indicated on Wednesday. Neutral means just that  $\hat{A}$ ? gold prices can rise or fall  $\hat{A}$ ? and that we are fluctuating above and below the 50 day moving average (\$1132) comes as no surprise. I also didn't detect any increase in commercial selling since the Tuesday cutoff. Given the neutral COT market structure in gold, we might be at a somewhat unusual juncture in gold (and silver) in that the various indications of tightness in the physical market just might exert more of an influence on price ahead. That's not something any of us have much experience with, but it is certainly not something to be feared.

In COMEX silver futures, the total commercial net short position increased by a scant 600 contracts, to 24,000 contracts. I had guessed no deterioration and was hoping for a reduction in commercial selling, but was close enough in terms of horseshoes. Commercial category changes were insignificant, as was the reciprocal side of managed money traders. While 10,000 contracts or so higher than what existed at the extreme lows in the total commercial net short position over the past month, on a historical basis, 24,000 contracts for the total commercial net short position is a bullish reading and close to 40,000 contracts less than what existed on May 19 (and \$17.50 silver)

Managed money traders sold 2310 longs, reducing the long side of this category to 37,735 categories, the lowest in a year and below my 40,000 contract core long position, although not by that much. This is not negative, as it just creates more room for buying when silver prices turn up. Managed money shorts did buy back 2553 contracts and I didn't want to see that many slip out the back with no price gain. However, it may not be all that bad if managed money traders have grown wary of selling short below \$15 in silver, as they've had very little success previously when shorting at such depressed prices. And if managed money traders are not inclined to add to shorts in silver below \$15, I'm hard-pressed to imagine who will sell in their place.

As I suggested in gold, the COT market structure in silver may take a backseat to developments in the physical market. I look forward to the day when prices are set by the actual supply/demand fundamentals and are not controlled by the manipulative price discovery process on the COMEX. Recognition of a problem must occur before the problem can be solved and this week I witnessed the spark of recognition like never before. This week, more than at any time before, I observed more commentary in which no known developments in the actual world of commodities could be attributed to price moves in metal and oil. I'm still waiting for the right reason to be given Â? price manipulation on the COMEX/NYMEX Â? but I feel the recognition is closer than ever.

### Freeport-McMoRan

The big news in the mining world this week was the disclosure that the famed activist investor, Carl Icahn, bought more than 8.5% of the stock of the oil and metals producer Freeport-McMoRan, investing a billion dollars. A day before the disclosure, the company announced a sharp cutback in capital expenditures and planned on reducing metal output, in reaction to the depressed price of copper, including the planned layoff of 10% of its US copper workforce, or 1500 employees and contractors.

<http://www.bizjournals.com/phoenix/news/2015/08/28/carl-icahn-takes-top-stake-in-freeport-mcmoran.html?ana=yahoo>

I have mentioned Mr. Icahn several times recently in connection with him being exactly the type of big investor that could give the price of silver a real shot in the arm. I did this even before Donald Trump suggested that Icahn would make an ideal Treasury Secretary. First, he's more than capable of investing one billion dollars or more in anything he chooses and he has the habit of letting the world know why he thinks any investment may be undervalued. Having just written an article describing how a billion dollars could be used to acquire 65 million ounces of actual silver and make billions of dollars, I can't help but feel that the day when someone follows my suggestion may be drawing near, whether it turns out to be Mr. Icahn or not.

But today, I'd like to focus on an issue even more serious and, unfortunately, quite ugly. Freeport is laying off 1500 US workers in response to the low price of copper which fell more than 70 cents a pound, or 24% from mid-May to the lows this week. In reaction to the fall in the price of the metal, Freeport stock fell more than 60% in value over this time (from \$22 to \$8), before rebounding slightly on the announced restructuring and Icahn's purchase.

Without a doubt, it was the sharp decline in the price of copper behind Freeport's actions and the loss of so many American jobs. The only real question is what caused copper prices to decline from May 19 until earlier this week? If you listen to commentators who are looking at the price decline first and finding the reasons afterward to explain that decline, it was related to some great oversupply of copper mostly linked to weakness in China. If you listen to those in the business of mining copper, like the CEO's of Glencore and BHP Billiton, there is no oversupply of metal. Further, Glencore's Ivan Glasenberg placed blame for the decline in the price of copper on hedge fund selling, much like I've intoned for months (if not years). And it's not just miners talking their own book; every serious research report I've seen also suggests actual copper fundamentals are close to being in balance.

Data from the CFTC, have documented that speculators in the managed money category have sold, since May 19, more than 70,000 net contracts of COMEX copper futures over that time, the equivalent of nearly 900,000 tons of copper or 18 days of world annual output. No other trader category on the COMEX even came close to selling as much as the managed money speculators sold, with the category identified as including producers, merchants, users and processors, actually buying nearly 60,000 net contracts.

In other words, there was no hedger selling possible (since those considered to be hedgers bought) and the purest and most speculative traders of all (those speculating with other people's money) were the overwhelming sellers. If there are no documentable facts pointing to an actual oversupply of copper and irrefutable evidence of massive speculative selling in COMEX copper futures, it would appear clear that the speculative selling drove prices lower.

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