December 11, 2019 – Occam’s Razor

If there is one question that Iâ??ve been asked more often than any other for many years (decades actually), it is why do the managed money traders persist in the apparent folly of falling for the dirty tricks and price prompts from the commercials in their COMEX gold and silver dealings? After all, there can be little question that the managed money technical funds, with their rigid approach of buying as prices rise and penetrate the key moving averages and selling when prices decline, are very much the enablers of the ongoing silver and gold price manipulation. Not the perpetrators, mind you, but surely the enablers.

Without the mechanical buying and selling of the managed money technical funds, the commercials (banks, led by JPMorgan) would not have held the death grip on price theyâ??ve held over the past 35 years or longer. And without the technical funds behaving so predictably over the years, we would not be at the zenith of interest and belief in the market structure premise, as highlighted by the Commitments of Traders (COT) report. If the managed money technical funds didnâ??t buy and sell on such a rigid and predictable basis, I can assure you that the COT report wouldnâ??t be worth a fraction of what observers have come to think of it.

Having had first hand experience with how the technical funds operated from the mid-1970â??s, when I first marketed and administered independent commodity trading advisors (CTAs) to clients as a broker, I answered the question about why they persisted in selling low and buying high in a number of ways. First, I would describe how the CTAâ??s were incredibly disciplined and stuck closely to their own programs, even if that meant going right back to a position that they lost on repeatedly, under the belief that the odds of success or failure on the next trade had nothing to do with previous trades (like tossing a coin 20 times in a row and getting heads, still left the 21st toss at 50-50).

Second, because the technical funds were extremely well-capitalized (over-margined) and only committed a very small percentage of total assets to any one trade, they were prepared to suffer lots of small losses in the hopes of attaining a few much larger gains (cutting losses short and letting profits run) by catching onto a developing price trend that would last for a long time. For instance, the technical funds might get chopped in and out of precious metals trades, but would profit from a few highly profitable trades in unrelated markets (like stock indices or bonds).

So predicable was the technical fundsâ?? behavior up until recently (the past few months), that their sudden refusal to sell anywhere near as aggressively of late strikes me as a seismic shift (as I wrote last week). The open question is why the sudden change in what has been a predictable pattern over decades? Iâ??ve speculated that perhaps JPMorgan whispered in the ears of select hedge fund clients, seeing as higher gold and silver prices are now aligned as being in the best interests of both JPMorgan and those managed money funds which donâ??t sell. Of course, thatâ??s speculation on my part, but in giving it further thought, perhaps thereâ??s a simpler explanation.

An English philosopher, William of Ockham, born in 1285, formulated the idea that the simpler the explanation, the more likely it was to be correct â?? which came to be known as Occamâ??s razor, derived from a Latin phrase (it has nothing to with shaving). Applying the term to the question of why the managed money technical funds have unexpectedly refused to sell aggressively in gold and silver of late where they have always sold previously, hereâ??s what Iâ??ve come up with.

Just like the simplest way to avoid the pain associated with beating oneâ??s head against a wall is to stop beating oneâ??s head against a wall; the simplest way for the technical funds to stop incurring the inevitable losses they have always collectively suffered in positioning COMEX gold and silver futures is to stop the past pattern of positioning â?? particularly when getting heavily short on declining prices. I donâ??t know what took them so long (it sure cost them a lot of money), but maybe, just maybe some technical funds finally woke up to the fact that they were the suckers sitting in on a crooked poker game. It doesnâ??t negate my speculation about JPMorgan selectively leaking out the word, but certainly if the technical funds objectively looked at their absolutely miserable track record in gold and silver over the years when shorting aggressively, they shouldnâ??t need much prompting to wake up and smell the coffee.

To be sure, not all of the managed money technical funds have gotten the word or awaken to reality, but enough of them apparently have â?? or at least thatâ??s what recent COT reports point to. Who knows, maybe some of these large traders came across my writings on the matter, but regardless, recent positioning points to some type of new awareness. Over the years, as regular readers know, I have referred to the technical funds as being brain dead, since they didnâ??t see that they were the enablers over which the commercials ran roughshod.

Since this has yet to play out, I suppose it is still possible that the managed money traders which have refused to sell to this point, might still end up selling aggressively on yet-lower prices. Were that to occur and the managed money traders which havenâ??t sold to this point on higher prices decide to sell aggressively on even lower prices that would make these traders look even dumber than the two characters in the movie, â??Dumb and Dumber.â?• As always, time will tell.

Since the main price driver for gold and silver has been the COMEX futures positioning between the managed money traders and the commercials, itâ??s impossible to overstate the impact of a radical change in the behavior of the technical funds. Itâ??s tantamount to the old rules being replaced, practically overnight. And since there always seemed to be a noticeable â??capâ?• on price rallies over the last three decades, inevitably followed by a flush out of the managed money traders to the downside, one canâ??t help wondering how a radically different positioning approach by the technical funds wonâ??t result in â??uncappedâ?• prices and the undoing of the concentrated short positions of the biggest COMEX commercial shorts.

I canâ??t help but note that as recently as this past April/May, the managed money traders held exceptionally large gross and net short positions in COMEX gold and silver futures â?? right at what proved to be the dead price lows ($1270 in gold and $14.25 in silver). It was practically impossible not to be wildly bullish on both metals due to COT market structure reasons alone. And sure enough, we had the strongest price rallies in years, as the managed money traders went on to buy nearly 300,000 net gold contracts (30 million oz) and 100,000 net silver contracts (500 million oz), pushing gold prices up by roughly $300 and silver by more than $5 into September. It was a text-book rally, driven nearly exclusively by managed money buying from a deeply oversold condition.

Since the September highs, prices have retreated by $100 in gold and $3 in silver, but for the first time in memory, the managed money traders have only sold a fraction of what they typically have sold in the past; only about 40,000 net contracts in gold and 15,000 contracts in silver (likely a bit more in Fridayâ??s new COT report). What gives â?? why hasnâ??t there been more managed money selling?

Could it really be that the managed money technical funds finally wised up and that things will be different from now on? That sure seems to be the simplest and most direct explanation for the recent radical behavioral change by these traders. That and what the heck took them so long?

Turning to other developments, a new thought occurred to me about the extraordinary circumstance of the explosion of Federal Reserve accommodation in the repurchase (repo) market that erupted in mid-September. Iâ??d be lying if I claimed to understand exactly whatâ??s going on, except to know that truly astounding amounts of money (many hundreds of billions of dollars) are involved and that certain facts seem clear. Most reports point to JPMorgan as being at the heart of the expanding repo drama. What follows is unadorned speculation about a possible connection between JPMâ??s role in gold and silver and the developing repo saga.

The Justice Department investigation into precious metals price manipulation by traders, both former and current, of JPMorgan must be considered mature at this point. The first guilty plea was secured more than a year ago and has been followed by another guilty plea and indictments of enough JPM traders to raise the question of whether there were any precious metals traders at the bank operating legitimately. The Justice Department has gone out of its way to label the precious metals desk at JPMorgan as a criminal enterprise and has used the RICO statute in bringing charges â?? virtually unprecedented actions. The DOJ has left unanswered the question of whether its allegations of a criminal enterprise apply to the traders or also to the bank itself. The answer to that question is beyond monumental.

I had come to the opinion that the Justice Department doesnâ??t have the chutzpa to charge JPMorgan as a criminal enterprise, not because the charge wouldnâ??t be fitting, but because of the widespread financial and economic damage that would result from the most systemically important financial institution in the US possibly being put out of business by such a serious charge. Any decision not to charge the bank itself still seems to me to be rooted in the fear of the unintended consequences on society in general that might result should the DOJ lower the boom on JPMorgan.

But perhaps Iâ??m wrong and the Justice Department has been acting tough with JPMorgan behind the scenes. Certainly, itâ??s virtually impossible that senior management at JPM could not have been aware of the widespread allegations of price manipulation in precious metals that have persisted since the bank took over Bear Stearns in 2008. After all, the protection of JPMorganâ??s reputation is an integral function of management, right up the Board of Directors level. In addition, Iâ??ve personally sent the bankâ??s CEO and board at least 1000 of my articles which explain JPMâ??s illegalities. Therefore, it is impossible that senior management at JPMorgan were unaware of the ongoing precious metals manipulation at the hands of its traders.

It is also certain that the Justice Department has been in close and constant negotiation with JPMorgan about the very serious charges of precious metals manipulation and whether to charge the bankâ??s senior management as being aware or complicit in the crimes alleged and from which guilty pleas have been secured. This puts senior management in the crosshairs, potentially liable for having their employment terminated or worse (ending up in the Big House).

Up until this point, I believe I have objectively described the situation that has developed over the past year and longer, without many, if any subjective embellishments. Iâ??ve just tried to connect the dots from the public record and what I know to be facts (like sending JPMorgan at least a thousand of my articles). Here comes the speculation. What if the DOJ, contrary to my take, has been much tougher on JPMorgan behind the scenes and has insisted on the dismissal or worse for high-placed senior management for overseeing the criminal enterprise on the precious metals desk? What possible counteraction could senior management take when faced with dismissal, the loss of personal reputation or worse (jail time)?

One of the few ways JPM senior management could fight back is by demonstrating just how important the bank is to the financial system and the economy and that the DOJ better tread lightly before charging the bank or its senior management as being complicit in the precious metals manipulation. What better way to do that than by throwing a monkey wrench into the repo market? Charge us and weâ??ll bring down the entire system. In other words, I believe the whole repo crisis was deliberately initiated by JPMorgan as a means to persuade the Justice Department to back off in charging the bank or its senior management in the precious metals manipulation. While this is, admittedly, unadorned speculation on my part, it is also simply the connection of several factual dots.

As far as what to expect in Fridayâ??s COT report, the sharp selloff in silver, on high trading volume, on Wednesday and Friday would seem to suggest notable managed money selling and commercial buying. There was only one real selloff in gold, on Friday, but trading volumes were not that heavy, meaning there was some managed money selling and commercial buying, but not of the earth-shaking variety. So I would expect more relative positioning change in silver than in gold (adjusting for the relative size of each market). Total open interest didnâ??t drop by that much (3500 contracts in silver and 11,000 contracts in gold), but it is always possible there were larger net changes in silver (since managed money long liquidation and new short selling would cancel each other out in terms of total open interest, but result in much larger net positioning changes).

Therefore, Iâ??m going to shy away from predicting positioning changes by numbers of contracts and instead focus on what has been the remarkable lack of aggressive managed money selling over the past few months. Regardless of what Fridayâ??s report indicates, it seems to me that the two days of sharp selloffs in silver this reporting week might be â??itâ?• as far as further aggressive managed money selling on lower prices (unless these traders are much dumber than I imagine).

I know Iâ??ve said it more times than Iâ??d care to recall, but the conditions for a moonshot in silver look stronger than ever. When I first discovered silver was artificially depressed in price by concentrated COMEX futures short selling in 1985 and knowing that it couldnâ??t last forever, Iâ??ve been waiting for the inevitable resolution. But along the way, even more bullish factors emerged that no one could have possibly foreseen.

Chief among them was the rise of JPMorgan as first the largest short seller on its acquisition of Bear Stearns in 2008 and the criminally-genius solution JPM came up with in 2011 to accumulate massive amounts of physical silver and gold. Hey, if you are going to artificially depress the price by excessive paper short selling, why not take advantage of the depressed price by buying physical metal? These boys at JPM may be crooks, but they sure arenâ??t dumb.

Therefore, the question has been for years â?? when will JPMorgan decide it owns enough physical metal to let prices rip to the upside? I canâ??t help but think that the recent refusal by the managed money traders not to sell where they have always sold before might be the answer to question. If the managed money traders have decided not to behave as before that means the fundamentals of the manipulation have changed â?? as in there is no good reason for the manipulation to continue. Or, at least, thatâ??s my take.

As far as the financial standing of the 7 big shorts in COMEX gold and silver, the rally through todayâ??s publication deadline more than erased last weekâ??s reduction in total open and unrealized losses to $1.8 billion, the lowest open combined loss in 4 months. Iâ??d peg the total open loss at this point to be back to $2.2 billion. I would also point out that despite last weekâ??s selloff, the 50 day moving average in gold is less than $5 higher than prices at this time.

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Silver – $16.95Â Â Â Â Â Â Â Â (200 day ma – $16.24, 50 day ma – $17.35)

Gold – $1481Â Â Â Â Â Â Â Â Â Â Â Â (200 day ma – $1408, 50 day ma – $1485)

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