December 7, 2016 – Clues Keep Coming

The Clues Keep Coming

I am still of a mind that we have recently experienced a masterful downward price manipulation in gold and silver that has set up the likelihood of a sharp rally. This has everything to do with the market structure on the COMEX, with particular emphasis on what JPMorgan is up to. I believe the rally will occur in the near future, although all timing predictions must be considered subjective and speculative and I can't rule out new price lows first.

Timing is always less of a consideration for long term investment than is good value or an attractive risk/reward ratio and presently silver has the best value and risk/reward profile I can recall. I know silver has been cheaper in price than it is currently, but the facts surrounding it have rarely been more compelling than they are now. I speak mainly, of course, in market structure terms Â? the current configuration of futures positions between the key players on the COMEX.

As I've been reporting, there have been some extraordinary positioning changes on the COMEX over the past three COT reporting weeks and, truth be told, I spend most of my time contemplating those changes. Please keep in mind that I don't always see all the changes upon the immediate release of the COT reports or appreciate their significance; that comes only after looking at the data from different angles and perspectives. And I'm not on the prowl for exclusively bullish factors, I'm just as interested in changes that might be bearish or differ greatly from long held premises.

One positioning change that I had thought about but forgot to write about was independently raised by a subscriber. Burt asked if the unprecedented lack of short selling by the managed money traders in silver didn't also mean that there was a lack of the type of potential short covering Â?rocket fuelÂ? from those traders that I've written about in the past. Since there is no question that if there is no big managed money short position in place, there can't be big short covering potential buying Â? that's simple math. Burt raised a point that needs to be addressed. So let's take it a bit further.

Without a doubt, every single time the managed money traders did go extremely short in COMEX silver (or gold), there was an inevitable price rally in which the short position was bought back. Over the past several years, this happened on numerous occasions, even allowing for the very few times some managed money shorts did get lucky and buyback before the rallies occurred. However, it is also true that while there were always price rallies on the numerous occasions of managed money short covering of an extremely large short position, none of those rallies were the Â?big rallyÂ? I speak of.

And there's no secret as to why no past occasions of strong managed money short covering resulted in the big move up in silver Â? commercial selling and new short selling was aggressive and sufficient enough to snuff out all the rallies. This is the essence of the Â?rinse and repeatÂ? cycle familiar to more each day. Had the commercials forced the managed money shorts to pay way up to cover shorts, silver prices would have exploded. But because the commercials always sold aggressively into managed money short covering (buying), silver rallies were mostly on the anemic variety.

My point is that the key feature of why the buyback of extreme short positions by the managed money traders (technical funds) never resulted in the big move up in silver had nothing to do with managed money traders' buying, but with the aggressiveness of the commercial selling. The managed money traders never failed to buy back large short positions as expected; the price determinant of the formula was the degree of aggression in commercial selling. Therefore, I'm not particularly concerned that there is no large managed money short position serving as potential rocket fuel at this time.

To be sure, all things considered, I would prefer there was a large managed money short position in place that needed to be bought back. But what I would prefer and what actually exists in this world are often two different things and I try to recognize that. Months ago, I opined that in order for there to be a complete reduction in the total commercial net short positions in COMEX silver and gold back to the extremely bullish levels that existed at year end, it was mandatory that there would be a large increase in managed money short selling.

That managed money short selling has not materialized and unless it does, I can't see how we get back to the headline bullish readings of year end. That's why I'm bullish now on the structure, even though a 75,000 contract headline commercial net short position in silver would normally look bearish beyond words. The bottom line on the lack of potential rocket fuel short covering from the managed money traders is that commercial selling on the next rally was always the key and still is. It is important to check and recheck every new fact in every way possible and I thank Burt for his thoughts. I'm not being corny when I say getting feedback from subscribers is always a treat.

Somewhat connected is another data point that struck me since the last COT report – the lack of raptor buying in silver over the past few weeks. Before I get into that, I believe this year's US presidential election set off some profound market moves; in stocks, bonds, currencies and, certainly, gold and silver. Markets that were weak going into Election Day, like the stock market, suddenly surged higher. The stock market set a record for consecutive declines going into the election, then set a record for consecutive advances after the election. On the other hand, gold and silver prices had been relatively strong going into the election, only to turn very weak afterwards.

Among reasonable people, there is always room for disagreement about why such market moves occurred; but not that the moves did take place. I'm sure every market has its own idiosyncrasies or mechanical conditions for what makes them tick, but I'm not well-versed on the specific workings of every market and that's why I usually refrain from discussing them. But I am as certain as can be that COMEX positioning moves gold and silver prices and there's little doubt in my mind why prices turned lower after the election, namely, a masterfully engineered positioning change.

As it turns out, there was a COT report in which the cutoff date was Election Day, November 8, for positions held as of the close that day, but before early election results began to roll in later that evening. Therefore, we got a snapshot of positioning as of the close that day and based upon the price action seen after the cutoff, we know there was heavy managed money buying and commercial selling that evening which was reversed into the next morning, Wednesday. We now know from subsequent COT reports that the managed money traders then sold many long positions in silver and gold (but added no short positions in silver) on the big price drop that began in the early hours of Wednesday, Nov 9 and continued through the most recent COT report ended last Tuesday, Nov 29.

I didn't notice it at first, but then it dawned on me that the raptors (the smaller commercials apart from the 8 largest commercials) did no net buying in silver on the price drop from Nov 8 thru Nov 29. On Nov 8, the silver raptors held a net long position of 11,600 contracts and that long position was reduced in each of the three subsequent reporting weeks to a 9300 net long position in last week's report. I'm not trying to suggest that 2300 contracts is a big number, as much as I'm suggesting that the raptors would have normally bought many more contracts under the price decline witnessed and not sold any.

Separately, I concluded in comments on the Nov 8 COT report that JPMorgan was short around 24,000 contracts on that date and subsequently, through the COT report of Nov 29, JPM had reduced its concentrated short position down to 18,000 contracts. The total commercial net short position declined by just under 7000 contracts from Nov 8 to Nov 29 and JPMorgan, effectively, accounted for 6000 of the 7000 total commercial shorts reduced. Never has JPMorgan bought back that large a percentage of the total commercial short position. I can assure you that my numbers are accurate, so let me suggest what this means to me.

Nearly a decade ago, I came up with the dinosaur analogy to describe the commercial traders in COMEX silver, patterned after the movie, Â?Jurassic ParkÂ?. To me, the 4 and 8 big concentrated shorts were the T. Rexes and the 20 to 30 smaller commercials were the velociraptors, the smaller, but quicker and pack-like dinosaurs which competed with the big guys over the same food supply diet of plant-eating reptiles. Interestingly, even though I wrote the article, Â?The Raptors,Â? long before JPMorgan emerged as the biggest and baddest silver T. Rex ever, in skimming the article today, I wouldn't change anything. (However, I did term the commercials as dealers and managed money traders as technical funds, as was my custom back then).

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Basically, I contended, back in 2007, that the smaller commercials, the raptors, were increasingly successful at poaching prey from the big T. Rexes because they were quicker to the punch and stepped in front of the big commercial traders when the technical funds came into the market to buy or sell. Thus, the raptors were quite successful in snaring profits away from the big guys as competition grew for a share of the managed money traders' largesse. By and large, that pattern prevailed until very recently. That it appears to have changed over the past three COT reports may be very big news.

The data over the last three reporting weeks indicate that the four big commercial shorts have stepped ahead of the raptors for the first time, as far as I can recall. To me, JPMorgan is, in essence, the big four, so it appears that JPMorgan is stepping ahead of everyone on the commercial side in buying silver futures contracts so aggressively. On its face, JPMorgan buying aggressively in anything is bullish; but silver isn't just anything. It is the most manipulated market in the world and JPMorgan has done nothing but buy the snot out of it for nearly six years running on a physical basis, while all along sitting on prices with a giant COMEX paper short position.

As such, it's the COMEX paper short position that controls the price and JPMorgan has been the key short seller over the past eight years; never failing to serve as the short seller of last resort in adding new silver short positions whenever needed to contain the price. Should JPMorgan decide to cease manipulating the price of silver it would cease adding new short positions and that alone would remove the price cap. Should JPMorgan decide to buy back as many of its COMEX short positions as it could, that would be a double bullish whammy.

The recent COT data indicate JPMorgan has been buying back some of its silver short position, so that only underscores and refines the specific question even more Â? will it add to silver short positions this time? I'm convinced that someday JPMorgan must stop adding to short positions on whatever is the next silver price rally and that will set the price on an upward trajectory not seen in silver before. Is that rally here or close at hand? I think so and, once again, apologize in advance if that doesn't turn out to be the case.

Another feature of the smaller commercials, the raptors, not buying over the past three reporting weeks is that their net long position is not large (at 9300 contracts) and that means less potential selling from them on a rally from here. Back at yearend, the raptors were net long 44,000 silver contracts as this year's price rally commenced, providing four and a half times the selling power they currently hold. If the big commercials, particularly JPMorgan, don't add aggressively to silver short positions, raptor selling wouldn't appear sufficient to cap prices. I suppose this is an offset or tradeoff to the loss of potential managed money short covering.

All the details under the hood suggest something may be afoot that may involve my long-held premise that JPMorgan could double cross the other commercial shorts in silver whenever it chose to do so. Maybe I'm imagining things, but at least my imagination is based on hard data from the COT report and elsewhere and for all the reasons I have given. It all adds up to a coming super surge in the price of silver. Please get back to me with any questions or thoughts you may have.

In other developments, the current COMEX December silver delivery period is starting to look a little Â?stickyÂ? in that there are more contracts still open than there are in gold, even though December gold open interest towered over silver at the start of the month. JPMorgan is still the largest stopper of silver deliveries and new issuances do not appear to be coming in sufficient numbers, creating the impression of physical tightness. With a suddenly interesting and different paper market structure, an injection of physical tightness only enhances the bullish setup.

This week, the CFTC announced some type of re-proposal for position limits that amounted to little more than the kicking of this can down a very long road in a place far, far away. The good news is that it was widely acknowledged that the Commission was simply avoiding dealing with position limits. At one time, thanks to former Chairman Gary Gensler, position limits actually stood a chance of being enacted, where today there is no conceivable chance of enactment. I will sooner play high school football again than will there be legitimate position limits in silver. The CFTC's announcement was akin to shooting an already dead horse. The good news is that position limits no longer matter in silver Â? all that matters is what JPMorgan does on the next (this) rally.

With yesterday's reporting week cutoff behind us, I can't offer much in the way of contract predictions for this Friday's report. The commercial short position headline number will probably be lower in gold, but silver's a tossup. Much more important will be the continuing details regarding managed money shorts, raptor longs in silver and, of course, where JPMorgan stands in silver and gold. Friday's release of the monthly Bank Participation Report will give me a chance to recalibrate JPM's short position in silver.

Today's rally has taken silver to price levels higher than any time over the past three weeks, in addition to penetrating the 20 day moving average to the upside. As you know, upward penetrations of silver and gold moving averages have been as rare as hens' teeth recently. Even absent the potential of big managed money short covering, the potential for big new (long) buying by the managed money traders is enormous and I have seen nothing to suggest that these traders won't buy (or try to buy) once moving averages are fully penetrated to the upside. As a result of today's rally, the key moving averages in silver are not as far above current prices as they seemed to be just a day ago.

It still comes down to the key question Â? will the big commercials, including JPMorgan add aggressively to short positions on this rally? Answer that correctly and the world of silver will be yours. I did come into today's rally fully expecting it could occur at any moment, although I can't tell at this point what JPMorgan may be doing. What I can tell you is that I am treating it as the start of the big move higher for the simple reason that to sell out too early in what may be the big silver move is something I cannot and will not do. If JPMorgan does turn big silver short seller again, I'll deal with that when it becomes known, not before.

Ted Butler

December 7, 2016

Silver – $17.25 (200 day ma – $17.69, 50 day ma – $17.59)

Gold – $1176 (200 day ma – $1280, 50 day ma – $1250)

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