February 20, 2019 – Icing on the Cake

Unbeknownst to me when I wrote last weekâ??s article, â??A New Silver Issue for the Justice Departmentâ?•, was the near simultaneous news that a leading silver mining company, Hochschild, had announced the closing of one of its Peruvian silver mines due to low silver prices. The Arcata mine, first put into production 55 years ago and reported to contain over 100 million oz in reserves, was said to produce around 4 million oz annually. There was little doubt that the decision to put the mine on care and maintenance was the result of continued depressed silver prices, despite the ten percent increase in price since Nov 13.

https://www.reuters.com/article/hochschild-min-operations/update-1-hochschild-mining-shuts-down-arcata-mine-in-peru-idUSL3N2082KY

The news announcement resonates for a number of reasons. In attempting to convince the Department of Justiceâ??s Antitrust Division to take up the matter of concentrated short selling on the COMEX silver futures market as being responsible for depressed silver prices, I made the point that it was absurd to conclude that the concentrated short selling was due to legitimate hedging by silver miners. Hochschildâ??s announcement underscores my point in that it proves silver prices are too low for legitimate producers to consider locking in by short sale on the COMEX. Instead, Hochschild took the painful but logical step of shutting down the mine until silver prices rise enough.

Since itâ??s clear that silver miners are not engaged in widespread bona fide hedging at current depressed silver prices to warrant their inclusion among the concentrated short sellers on the COMEX, then itâ??s imperative to ask then who is responsible. Thanks to unmistakably clear data from the CFTC in the form of disaggregated Commitments of Traders (COT) and Bank Participation reports, there can be little doubt that the concentrated short sellers are domestic and foreign banks â?? not miners.

The way it works is like this â?? the speculating banks (which are merely betting against the managed money speculators) pretend to be hedging and the CFTC accommodates this subterfuge by agreeing to classify the banks in the Producer/Merchant/User/Processor or Swap Dealers categories despite the obvious fact that the banks are speculating. Since there is always an ample supply of observers (not a one with hands on professional futures experience) who will glibly agree that anyone classified as a commercial is automatically engaged in legitimate hedging, regardless of clear evidence to the contrary, the con lives on.

What makes the silver manipulation con of speculative concentrated short selling so egregious is that the short sellers pretending to be legitimate commercial hedgers are hurting the very participants which should be hedging, the miners. That would likely occur if the price of silver was anywhere near where it should be in true free market conditions. Our regulated commodity futures markets were created and designed for legitimate hedgers to lay off risk through bona fide hedging. Instead, a handful of speculating banks and managed money traders have completely usurped the legitimate hedging function and have taken control of the pricing process. Not only is the price being set artificially by outsiders, the resultant price is most damaging to the market participants that futures trading was intended to benefit.

One of the reasons the matter of concentrated short selling in COMEX silver futures has gone by almost unnoticed all these years and is rarely commented on, even to this day, is because most commentators and observers donâ??t know how to calculate the concentration data. I believe thatâ??s because it takes a bit of hand-calculating to derive at the concentration statistics. While the data are precise to the exact contract, the COT report doesnâ??t present the data in contract form, only as a percentage of total open interest; leaving it to the observer to multiply the total open interest by the percentage of concentration given. As Iâ??ve written previously, the percentages given for the net short positions of the 4 and 8 traders are the only numbers that matter.

A reason the concentrated short position in COMEX silver futures may have escaped the notice of the Antitrust Division of the DOJ is because most price-fixing and monopolistic activities it deals with are of the variety that artificially boost prices to the detriment of the consuming public. But the reason that the statue of Lady Justice is blindfolded is because the law shouldnâ??t distinguish between artificial price-setting of either the higher or lower variety. The efficient functioning of free markets depends on the law of supply and demand not being distorted by artificial pricing of any kind. Any market artificially depressed in price may give users and consumers some advantage in the short term, but the eventual end to the illegal artificiality will lead to much higher prices in the long run.

In fact, itâ??s quite understandable that the Antitrust Division has not focused on the monopolistic pricing in COMEX silver futures. After all, there was created and exists a specific primary federal regulator, the CFTC, whose main mission is to prevent manipulation. In addition, there exists a designated self-regulating organization (SRO), the CME Group, also charged with the preventing of market manipulation. Normal protocol would suggest that matters pertaining to allegations of manipulation would be the province of the CFTC and the CME.Â If either regulator had fulfilled their prime responsibilities, there would be no need for Antitrust Division intervention. Sadly, thatâ??s not the case.

In any event, it is particularly pernicious when prices are set artificially by participants not involved with or even interested in the actual production or consumption of silver. Speculating banks or managed money traders couldnâ??t care less about the plight of actual silver producers, consumers or investors â?? they are just out to make a quick buck off each other in some massive private betting game on the COMEX sanctioned by the CFTC and CME Group. The problem is the private betting game is what sets prices and that â??outsidersâ?•, not actual producers and consumers run the game.

The closing of a not insignificant silver mine that has produced for more than half a century and appears capable of producing for another 50 years due to low prices is a timely reminder and confirmation that silver prices are unreasonably depressed. Thatâ??s why it is so potentially significant that the Department of Justice has stepped into the matter with an ongoing investigation by its Criminal Division, the FBI and the US Attorneys Division of COMEX precious metals trading. The Antitrust Division has every reason to join in as well.

As if to underscore the matter, yesterdayâ??s release of the still delayed Commitments of Traders (COT) report featured notable increases in the concentrated short positions of the 8 largest traders in both COMEX gold and silver. The increases demonstrate beyond a doubt that concentrated short selling is all that prevents sharply higher prices for both gold and, particularly silver. Itâ??s not just that the reporting week ended Jan 29 featured managed money buying and commercial selling, which was fully expected given the sharp price rallies that took place, but it has become increasingly clear that without concentrated commercial short selling prices would have rallied much more.

As of the close of business Jan 29, the commercials increased their total net short position by 26,500 contracts to 118,600 contracts, as the price of gold traded and closed decisively above $1300 for the first time in ten months, trading as high as $1310 on the cutoff day. Considering that the reporting weekâ??s close was up $110 from the price lows of Nov 13, the overall COMEX gold market structure was still much more bullish than I would have imagined at this stage. But the standout feature of the report was the sharp increase in concentrated short selling.

The 8 largest concentrated gold shorts, apparently all commercials, accounted for 20,000 contracts of the total commercial net selling during the reporting week. As of Jan 29, the 8 largest gold shorts hold a concentrated net short position of 187,072 contracts (18.7 million oz) versus a total commercial net short position of 118,600 contracts. While it is certainly typical and even â??normalâ?• for the concentered short position of the 8 largest traders to be much higher than the total commercial net short position, it is only normal in a manipulated market, which is a state the COMEX gold futures market has been in for many years. Thatâ??s because COT data prove that without the concentrated short selling by 8 speculating banks, there would be no net commercial short position at all (since away from the 8 largest traders, the commercials are net long).

One doesnâ??t even need to prove that these 8 big short banks have actively colluded to depress and contain gold prices â?? their documented short positions speak for themselves. If these 8 crooked banks hadnâ??t sold short 187,000 net contracts, gold prices would be much higher. Thatâ??s because all futures contracts need both a buyer and seller; so if the 8 crooked banks needed to be replaced by other sellers, unless one could find another 8 short sellers to replace them at current prices (an impossibility), then it would take many more traders for replacement. The only way to do that (conceivably) is through much higher prices. This is the central theme, but let me finish the COT report before coming back to this.

The managed money traders in gold bought far fewer net gold contracts than the commercial sold (always a good sign); 16,187 contracts to be precise, consisting of new longs of 21,109 and the new short sale of 4992 contracts. Explaining why managed money buying was less than commercial selling, was the nearly 9000 contracts of net buying by other large speculative traders. The net long position of the managed money traders of 32,000 contracts as of Jan 29, while higher by around 110,000 net contracts from the Nov 13 price lows, still leaves room for as many as 200,000 additional net contracts to reach the extremes seen in both 2016 and 2017.

In COMEX silver futures as of Jan 29, the commercials increased their total net short position by 7500 contracts to 72,500 contracts. This was in the expected range given silverâ??s three day price jump of as much as 60 cents into Jan 29. However, silver had yet to penetrate $16 by reporting weekâ??s end (it would do so in the report to be published on Friday). The short position of JPMorgan appears to have increased to 21,000 to 22,000 net contracts, while the concentrated short position of the 8 largest traders (definitely now all commercials) increased by 3000 contracts to 96,278 contracts, the equivalent of more than 481 million oz.

Please consider this. An underground mine in Peru that digs out of the earth 4 million ounces in a year was just shut down due to low silver prices; yet at the same time and price, 8 crooked banks have increased their net speculative short position to more than 100 times that mineâ??s annual production. If the Justice Department doesnâ??t see something drastically wrong with that, then all hope for the rule of law is lost. Remember, concentration is the one absolute requirement in any manipulation. In silver, the concentration is off the charts.

You have to go back to last summer to find a larger concentrated short position in silver, but even when you do, some big differences are obvious. For one, JPMorganâ??s short position was larger then, while the short position of other commercial traders (swap dealers) back then was smaller than it is now. What I think this reflects is JPMorganâ??s move to be done with manipulating the price of silver and it quietly passing the hot potato to the other big commercial shorts. I further believe this could prove to be the ruin of the other big commercial shorts that will soon be evident in an explosive price move higher. Dead men walking, indeed.

The managed money silver traders bought less than the commercials sold (same as in gold), in buying 4746 net contracts, consisting of 3230 new long contracts and the buy back and covering of 1516 short contracts. Even though the managed money traders in silver have bought more than 80,000 net contracts (400 million oz) since Nov 13, much more proportionately than the 110,000 net contracts they purchase in gold, there is still room for as many as 60,000 net contracts of additional managed money buying (and, admittedly, even more room for selling to get back to Nov 13 levels).

If you hadnâ??t noticed, I keep referring to price and market structure levels since Nov 13. The reason is because I think the world of silver and gold may have changed because of the shocking announcement by the DOJ on Nov 6 that it was investigating precious metals manipulation on the COMEX. Letâ??s face it â?? as of today, just over three months later, gold has now rallied by as much as $150 and silver by more than $2, with nary a spoofing price take down in the interim. Itâ??s either a remarkable coincidence or something more. Count me in the â??something moreâ?• category.

I continue to believe that the fate of the 8 concentrated shorts in COMEX silver and gold holds the key to what occurs next, namely, these big manipulative traders will, yet again, succeed in knocking down prices and buying back added shorts at lower and profitable (to them) prices or they will fail spectacularly for the first time ever. While this is a clear either or circumstance, the consequences of the big shorts failing for the very first time loom larger in my opinion than ever before. The only way in which I can explain that is by my money scoreboard tabulation, which I hadnâ??t raised very recently because prices hadnâ??t done much since my calculation on Feb 2.

Just to be clear, I include JPMorgan in the calculation for how the big 8 shorts are doing in gold and silver on a combined basis, but I hope you know that JPMorgan, by virtue of its massive physical holdings of silver and gold (800 million oz and 20 million oz respectively), is completely immune from real losses on its short positions on an explosion in gold or silver prices. JPMorgan is in great jeopardy from Justice Department findings, just not market losses from higher gold and silver prices.

Itâ??s a much different situation for the other big gold and silver shorts, which are completely exposed to unlimited losses on the short positions they hold. Certainly, JPMorgan is nowhere near as short as it has been in the past and thatâ??s an indication to me that the big remaining commercial shorts are no longer the cohesive â??all for one, one for allâ?• unit that existed in the past. In fact, the only question in my mind is if these other big shorts actually realize the danger they are in or are they about to learn it ahead on a first hand basis. I think I do understand why these big shorts would have put themselves in such a dangerous situation, namely, it always worked for them before. But that was before JPMorgan abandoned ship and the DOJ began nosing around (likely one and the same). But COT data indicate clearly that the big shorts have committed themselves to the short side, wittingly or unwittingly.

So now the question is how much financial damage the big shorts, ex-JPM, can and will take before one or two (to start) break ranks and, in turn, weaken the collective death-grip on prices always held by the big 8 shorts. This is where the money scoreboard calculations come in handy. Back on Feb 2, when I resumed the calculations after a long absence, I calculated that the big 8 shorts, on a combined basis in silver and gold, were out $1.3 billion. That was based upon a 20 million oz short position (200,000 contract) in gold and a 400 million oz short position (80,000 contracts) in silver and using a gold price of $1322 and silver price of $15.92. I had calculated on Feb 2 that the average price (cost basis) for the big 8 short position to be $1275 in gold and $15 in silver.

Updating the variables for latest reported positions (19 million oz in gold and 480 million oz in silver and the slightly higher average shorting price ($1280 in gold and $15.20 in silver), at todayâ??s prices ($1345 in gold and $16.10 in silver), the combined open loss for the big 8 traders in both gold and silver is just under $1.8 billion, up nearly a half billion dollars since Feb 2.

The previous high-water mark for the maximum dollar amount the big 8 shorts were in the hole for on an open and unrealized basis was approximately $4 billion in the summer of 2016, when gold hit $1385 and silver was over $21. That time, the big commercial shorts prevailed and just after Election Day 2016, the commercial shorts recouped all their open losses. While that possibility must be said to exist today, there are some important differences between the summer of 2016 and now. What are those differences?

For one, the current move higher is relatively young, just over three months in existence, while the move in 2016 was two or three times more mature. In addition, gold prices are not that far from its peak prices of 2016, while silver is still miles below its $21 former high. Also, the concentrated gold short position in back at the peak in 2016 was 100,000 contracts (10 million oz) larger than it is now; I believe due to the much larger rally that took place in 2016, when gold rose around $300 to the peak (versus $150 in the current move).

However, the biggest differences today are that JPMorgan is no longer the stalwart and backbone of the concentrated short position as it was back in 2016, meaning there is a greater propensity for the remaining shorts to panic and rush to cover at some point than they were back then; plus one other thing. That â??other thing,â?• of course, is that there was no Department of Justice ongoing investigation in place back then, as there surely is now.

I donâ??t think the big shorts, away from JPMorgan, have a clue as to what type of exposure they have placed themselves in by virtue of what they have shorted to date â?? otherwise they wouldnâ??t have shorted in the first place. I believe, as is customary in any DOJ investigation that subpoenas have been issued and depositions have occurred; but that those subpoenas and depositions have been confined to JPMorgan and do not include the other banks wildly speculating in COMEX gold and silver futures. Yet.

That leaves open the distinct possibility that the other big shorts might learn the hard way about what a predicament they are in. The â??hard wayâ?• involves a sudden recognition that the gold and silver rally have run far enough for them to do anything but starting to buy back and cover shorts to limit losses as quickly as possible. That translates into sudden and aggressive buying in markets in which they have been the primary short sellers. That leaves open the question of who the heck might sell to the newly panicky shorts desperate to buy and at what price? Yes, Iâ??m talking about the possibility of a price explosion and the mechanics for why it might happen.

Finally, a month ago, in the weekly review of Jan 19, I mentioned the futures market structure of a number of markets, including copper, palladium and crude oil. In copper, I mentioned that the managed money short position was likely near a record and most likely to unfold in a â??hellaciousâ?• rally. Over the next week, copper prices fell anew (making me feel like a jerk for bringing it up). However, after the subsequent price low of $2.63, copper prices have rallied to over $2.92 today. I donâ??t know if that meets the definition of hellacious, but it is the highest price copper has seen since last July. I do know that the prime driver for the rally has most likely been managed money short covering. It sure hasnâ??t been economic reports indicating an uptick in actual copper consumption.

In mentioning palladium, I commented how the managed money net long position had likely hardly changed since Dec 18, since total open interest had not changed much. The COT report of Jan 29 confirms that the net and gross long position of the managed money traders has hardly budged in NYMEX palladium futures. This means that whatever drove palladium prices to new highs (up more than $250) was something other than managed money buying. The most likely â??something otherâ?• was physical buying by industrial users, not speculators. Iâ??m not predicting what palladium prices may do, just that there is scant evidence that the rally is being driven by speculative buying in futures markets.

As for crude oil, I mentioned that the managed money long position looked historically low and most likely to increase in time, driving prices higher. While crude oil prices are a few dollars higher amid some signs of managed money buying (mostly short covering), itâ??s far too early to conclude whether my take will be correct. But, hopefully, the Justice Department will take a strong look at what really sets the price of many commodities.

Ted Butler

February 20, 2019

Silver – $16.10Â Â Â Â Â Â (200 day ma – $15.30, 50 day ma – $1542)

Gold – $1345Â Â Â Â Â Â Â Â (200 day ma – $1251, 50 day ma – $1288)

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