July 23, 2016 – Weekly Review

Weekly Review

Following six weeks of higher closes, gold and silver prices fell for the second week running, with gold down $14 (1%) and silver off by 50 cents (2.5%). Gold's relative outperformance resulted in the silver/gold price ratio widening out by nearly a point and half to just under 67.5 to 1.

I don't think there is anything that would surprise me about short term changes in the price ratio, but I will be very surprised if silver doesn't vastly outperform gold in the long term. About the only thing I think I do know about the price ratio is that virtually no one actual exchanges meaningful quantities of one metal for the other on a regular basis Â? the changes in the ratio have everything to do with COMEX paper trading and little else. In fact, it is just such paper price setting that has created the incredible relative undervaluation in silver compared to gold.

Therefore, trying to read too much into the relative merits of gold and silver by short term changes in the silver/gold price ratio is a wasted exercise, in my opinion. As is trying to read too much into short term price fluctuations of any sort. Yet there are plenty of short term price gyrations of the type we witnessed this week that do warrant some attention and I'll discuss this after running through the usual weekly format.

The turnover or physical movement of metal brought into and removed from the COMEX-approved silver warehouses totaled 4.9 million oz this week. Total inventories rose for the second week running, this time by 2.7 million oz to 155.4 million oz, 5 million oz more than the levels of two weeks ago. Total COMEX silver warehouse inventories are still much closer to the lowest levels over the past three years, but I mention this only to keep things in perspective; my interest is still on the turnover, not the totals.

The fact still remains that the physical turnover in COMEX silver inventories stands out like a sore thumb when compared to all other commodities. An average of 5 million oz weekly equates to 30% of total annual world silver mine production and why in the world would 30% of the annual world production of any commodity need to be physically moved about in and out of six warehouses in and around New York City? And why would this unprecedented physical turnover persist for more than five years? My answer, of course, is that it represents a chief source of the physical silver JPMorgan has accumulated over this time. Other suggestions, of course, are always welcome.

The July COMEX silver delivery period is winding down in the same manner it has progressed for the month, namely, with JPMorgan in second place as the biggest stopper after HSBC. JPM still looks set to take around 800 contracts (4 million oz), while HSBC should take a total of 1100 contracts by month's end. This marks the first time that JPMorgan has not been the big COMEX silver stopper in a year and a half. Combined with JPM's complete backing off from buying Silver Eagles, I can't help but feel that the bank is setting the stage for a silver price lift off by trying to quietly refrain from buying silver aggressively to cut down on awareness of its accumulation to date. However, this is a process of undetermined time limits.
http://www.cmegroup.com/delivery_reports/MetalsIssuesAndStopsYTDReport.pdf

Switching to the COMEX July gold deliveries, a customer(s) of JPMorgan has now taken more than 4400 contracts (440,000 oz) in what has always been a traditionally inactive month. Most likely, the same JPM customer(s) took 4000 contracts in the June delivery process, in which JPMorgan took 6700 contracts for its own account. That's a two month total of more than 15,000 contracts or 1.5 million ounces of gold Â? 15% of total COMEX gold inventories. And the big COMEX August gold delivery process begins next week.

The word Â?extraordinaryÂ? does not adequately describe these levels of COMEX gold deliveries. In fact, about the only thing not extraordinary about the massive size of the gold deliveries is JPMorgan's involvement. This involvement should help remove any doubt that JPMorgan is numero uno in the world of gold and silver. So much for all the talk about getting banks out of the commodity trading business. Instead, even the supposed hard position limit of 3000 contracts in the spot month has become a standing joke as it has been exceeded so often recently.

Still, the large recent and prospective COMEX gold deliveries raise many questions to which I have few answers. I understand the main price driver for gold and silver this year has been the historically large buying by the technical funds on the COMEX. I also understand how the resultant price advance triggered massive buying in mining shares and metal ETFs, which resulted in large deposits of physical metal, particularly into the big gold ETF, GLD.

But I am at a loss, at least for now, as to what these massive COMEX gold deliveries are all about, aside from knowing JPMorgan and its customer(s) have aggressively acquired physical metal above and beyond anything seen previously. I know my initial reaction is that it must be bullish for the price (as who buys anything with no expectation of higher price), yet I've detected no bullish price impact from the deliveries to price to this point. Sure gold and silver have moved higher this year, but I can't attach the massive COMEX gold deliveries to being the driving force.

I know that JPMorgan has apparently moved the gold it took delivery of in June (around 650,000 oz) to its own COMEX warehouse, following the pattern it established in silver, but I have detected no movement of the metal its customer(s) acquired. Not that there must be a movement of metal following deliveries, as the new owners may be content to store the metal as is and where it sits.

As impressive as the amounts of physical gold JPM and its client(s) have taken, it also is very impressive the amount of gold provided with no apparent stress. Some believe, of course, that metal deposits into GLD (or SLV), as well as anything COMEX-related can't be trusted, but I am not remotely in that camp. Serial numbers and specific weights are always published for each gold or silver bar deposited into GLD or SLV and the sponsors of each trust (State Street and BlackRock) would have nothing to gain and everything to lose for any misrepresentation. And since JPM has been the prime stopper in COMEX silver for more than a year and a half and more recently in gold, it's not like the bank is trying to hide its accumulation. Sometimes the data are reliable and visible and yet firm opinions about the data can't be reached. As always, it's more important to recognize the meaning of the data rather than the data itself. I don't know the true meaning of the COMEX gold deliveries yet, but hope to in time.

As alluded to above, sales of Silver Eagles continue to stink, with July possibly shaping up to be the weakest month in years. Ironically, the start of the month featured a sharp pickup in retail sales following the July 4 price fireworks, so this month's slow sales are particularly noteworthy. Unlike not knowing what the data may indicate with COMEX gold deliveries, the meaning of the falloff in Silver Eagles sales means one thing Â? JPMorgan has stepped back completely in its five year acquisition of the coins. I believe JPM will either reinitiate its accumulation of Silver Eagles at lower prices or is setting the stage to be as inconspicuous as possible before the silver price liftoff. Who knows Â? maybe someone in the new administration to come this fall might inquire why the nation's largest bank has been the largest buyer of Silver Eagles for five years?

http://www.usmint.gov/about_the_mint/index.cfm?action=PreciousMetals&type=bullion

The changes in this week's Commitments of Traders (COT) Report were dramatic in silver, but less so in gold when measured against price performance during the reporting week. Silver and gold prices were mostly flat to lower during a reporting week featuring somewhat lackluster trading volumes. As such, gold's reduction of 10,000 contracts in the total commercial net short position looked in line, while silver's big 6000 contract increase looked out of step.

In COMEX gold futures, the commercials reduced their net short position by 10,000 contracts, to 315,500 contracts, bringing to nearly 25,000 the number of commercial shorts closed out over the past two weeks. The problem is that despite the reductions, anything close to 300,000 contracts of net commercial shorts leaves us still in nosebleed bearish territory, by a hundred or two hundred thousand contracts. Therefore, it is still very safe to say that the resolution of the most extreme market structure in history still lies ahead for gold and silver.

By commercial category, the 4 big COMEX gold shorts bought back 2300 contracts and the big 5 thru 8 gold shorts bought back 3800 contracts (following last week's big increase). This left the raptors (the smaller commercials apart from the big 8) buying back 3900 short contracts. Clearly, the Â?all for oneÂ? memo was received this week. On the sell side, the managed money traders sold 6732 net gold contracts, including 8789 contracts of long liquidation. We are only slightly off from the record extremes of commercial shorting and managed money buying. How we move away from those extremes eventually will be the prime price story to come.

In COMEX silver futures, the commercials increased their total net short position by a very hefty 6100 contracts to 106,300 contracts, another record for the ages. Never before has there been such a large commercial short position or such a large managed money long position or most importantly, such a large concentrated short position, which this week climbed to more than 100,000 contracts or 500 million oz.

Eight traders are now net short more than 500 million oz of silver or an average of 62.5 million oz per trader. No silver mine or silver mining company comes close to producing such an amount of silver annually, but then again there is no evidence that any silver producer holds any appreciable amount of the COMEX concentrated short position in any regard. That's what makes the concentrated short position manipulative on its face.

A subscriber asked me this week about the concentrated long position in silver and whether that long position wasn't a problem as well. The short answer is that yes, it is a problem. The eight largest long traders hold a net long position of 66,000 contracts or 330 million oz; an average of 41 million oz per trader. While smaller that the concentrated short position, just like it, there is not the slightest evidence that there is a non-speculative aspect to the concentrated long position. The concentrated long position, just like its short counterpart is purely speculative and involves not the tiniest bit of legitimate hedging (which is the reason Congress authorized commodity futures trading in the first place.

Moreover, US commodity law forbids excessive speculation in commodity trading from setting prices, while there is nothing about trading in COMEX silver and gold that isn't excessive speculation. All the trading is speculative and not legitimate hedging. Both the concentrated short and long positions in COMEX silver make a mockery of any suggestion that the price of silver (or gold) is set by real world supply and demand.

The solution to the excessive speculation on both the short and long side of COMEX silver and gold, as I have long advanced, is legitimate position limits on individual traders and a collective limit on those traders which operate as one (technical funds). Since such an imposition of legitimate position limits would undo the price manipulation, it stands no chance of being enacted. But it is important to know this problem could easily be fixed if the regulators weren't corrupt. I'm still waiting for the first rebuttal to my contention that concentration is the key factor.

All that said, I don't believe the concentrated long position is deliberately manipulative, just as I know the concentrated short position is deliberate, based upon the mechanics by which each side operates. The technical funds are trying to catch and add to a trending market; the commercials are simply out to frustrate and exploit the technical funds. The sooner everyone realizes this, the nearer we'll be to the manipulation's end.

By commercial category, the 4 big shorts in silver added 2300 contracts to a net short position now at a records 70,365 contracts. I'd peg JPMorgan's share to be 32,000 contracts or 45% of the big 4 concentrated short position, but will need to wait to the Bank Participation Report in two weeks to be sure. The big 5 thru 8 shorts added 600 new short contracts, while the raptors added 3200 new short contracts to a net short position now amounting to 5700 contracts.

On the buy side in silver, the managed money traders added 5969 new longs, just about equal to all of the commercial contracts sold and established new record net and gross long high water marks.

There was something about this week's silver COT report that I found disconcerting, if that is the right word. What troubles me is that the price action and trading volumes during the reporting week were lackluster and not in keeping with the large reporting jump in commercial shorts and managed money longs. As a result, I'm a bit confused about the aggression on both sides. Normally, 6000 contracts of new technical fund longs would occur concurrent with clear new price highs (salami slicing), but that didn't occur in this reporting week. What I'm confused about is what made the commercials so aggressive in selling this reporting week that the rally was, more or less, so snuffed out as to appear to be non-existent. Like the questions surrounding the COMEX gold deliveries, this puzzle will hopefully be answered in time.

I mentioned I would address the meaning behind sharp intraweek price moves earlier. In fact, it's something I've been meaning to address for some time. Specifically, what accounts for the sharp up and down price moves this week or any time? Since I believe the main price driver is COMEX positioning, you won't be surprised that I call on that as explaining short term moves as well. From everything I've observed over the past three decades, it's safe to say that the managed money technical funds buy on rising prices and sell on falling prices, with penetrations of moving averages and a succession of either new highs or lows particularly influencing the degree of technical fund aggression. The commercials, of course fade the technical funds on either side of up and down price movements.

So consistent is this mechanical description of technical fund/commercial behavior that sudden price rallies are likely due to technical fund buying and any selloff is likely technical fund selling (of course, engineered by the commercials). In other words, the daily price movements are likely governed by the same mechanical forces that determine intermediate term price movements. Let me put it this way Â? I don't believe the technical funds are selling on sudden price moves higher, with the commercials as buyers. I believe the commercials are and have whipsawed the technical funds on a daily as well as longer term basis.

This is largely borne out in the continuing flow of COT data, although this week's silver report was unusual. My point here (at least up until now) is that the commercials zoom the technical funds any which way they can and on every time frame in question. This is something to be kept in mind as I give my running financial scorecard updates in that the scorecard is likely more favorable to the commercials than I relate. I believe the commercials victimize and profit off the technical funds in very short term trading, rather than the other way around.

Of course, with the extreme market structure, a fairly dramatic resolution would appear to be close. Either the technical funds will get liquidated to the downside as they have over the years or the commercials will get overrun for the first time ever. I still lean to some measure of technical fund selling before we move higher in silver for real, but my Â?leaningsÂ? don't matter for much. I know there are those calling for the commercials to be overrun for sure and just as many calling for prices to surely sell off. I envy those who know for sure, but don't count myself in either camp. I'm waiting for more attention to the concentrated nature of positioning.

Gold and silver finished slightly higher than my last financial scorecard update on Wednesday, but still down for the week. That means since the last weekly review, the commercials have whittled their bottom line soup to nuts combined open loss in COMEX silver and gold this year by a bit over $600 million from last week's $1.5 billion loss and from the $2.5 billion the commercials were out at the gold and silver price highs of three weeks ago. Normally one shouldn't count the money while the game is still being played, but it's not my or your money that I'm counting, just that of the two competing trading groups on the COMEX. It still seems to me that that's the count that matters most.

Ted Butler

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Silver – $19.70   (50 day moving average – $17.95)

Gold – $1323   (50 day moving average – $1290)

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