July 25, 2015 – Weekly Review

Weekly Review

For the fifth week in a row, gold and silver prices fell, although prices did rebound in late Friday trading after establishing new five year lows earlier. For the week, gold ended $34 (3%) lower, while silver ended down 15 cents (1%). The silver/gold price ratio tightened in by nearly two full points to just over 74.5 to 1, reflecting silver's relative outperformance this week.

I try to avoid reading too much into short term price changes, but it is very rare to see silver stronger on a relative basis to gold on overall price weakness. While short term price action is low on my list of what the future may hold, there are enough other factors in place to suggest that both metals will soon be heading higher, with silver expected to lead the way.

New multi-year price lows in gold and silver have become a regular occurrence recently and I'd like to offer some personal observations before getting into the usual weekly format.

In the more than 40 years I have been observing the financial scene (having started as a stock/commodity broker at Merrill Lynch in 1972), I have never witnessed such an outpouring of negative commentary as I have seen recently on gold. To be sure, gold currently has to be the most hated asset of any kind over the past four decades, unless my memory is seriously out of kilter. (I'm sure silver would also be hated by those issuing condemnations on gold if asked and the only reason it's not mentioned is due to it generally being ignored anyway.)

I'll not belabor the point, but extremely held collective opinion is perhaps the strongest market contra-indicator of all. Important price bottoms in any asset class are always accompanied by collective feelings of despair and expectations of certain lower prices to come; important market tops feature near universal optimism. Judging by the near-universal negative commentary on gold, it must be considered a buy on that basis alone. But there some other things related to this outpouring of negative gold commentary that I'd like to get off my chest.

There appears to be a great dichotomy between how the traditional main stream media (Wall Street Journal, Bloomberg, Reuters, CNBC, etc.) reports and opines on the recent gold price decline compared to the more upstart Internet sites covering the metals. Further, there also appears to be a growing number of commentators within the upstart Internet precious metals community who have come, like never before, to the conclusion that futures positioning on the COMEX determines price; some quietly implying manipulation for the first time ever (without using the dreaded Â?M' word).

Since I try to read everything available on this issue, I have been working overtime trying to keep up with the outburst of negative commentary on gold. As always, I am more interested in the reasons behind anyone's opinion of future prices and not the opinion itself (I do try to adhere to that principle on these pages). I can tell you that while the (negative) opinions are strongly stated in mostly no uncertain terms, the actual reasons backing those certain opinions are shaky at best, or completely lacking. It's mostly a case of gold has gone down and that means it will continue to go down for all the same reasons always given (no inflation, the dollar, the stock market, etc.). In addition, most of this commentary comes from those who don't devote all their time to studying precious metals.

In contrast, the upstart Internet sites have been increasingly zeroing in (no pun intended to the coming reference) on what I have always contended to be the true prime cause of price movement Â? COMEX futures positioning. I'll get into this week's COT report in a moment, but here's an example of an upstart Internet site's coverage on the new report from Zero Hedge that has already attracted more than 180,000 views.

http://www.zerohedge.com/news/2015-07-24/has-never-happened-gold

What's remarkable about this article is that it is so brief and to the point and in providing instant analysis of yesterday's report, automatically focuses on the most important gold price driver. There was also a widely read post on Zero Hedge earlier in the week that made the COMEX futures positioning connection with the Sunday night price smash. I fully admit to being strongly opinionated about the COMEX's price setting in metals because this is the nexus of the price manipulation, but this is much more than agreeing with people who agree with me.

Instead, the COMEX connection is the only verifiable, measurable and objective explanation of gold and silver price movement and it's only a matter of time before that is widely recognized. The wonder is that the discovery of the true price driver has grown like wildfire within the Internet community and now threatens to jump the firebreak that has somehow prevented the idea from being discussed within the main stream media. Don't get me wrong Â? I know increasing reference to the COT report is being made within the main stream media, but not (yet) to the unavoidable conclusion that speculators on the COMEX are illegally setting prices.

But I do think a much wider discussion of COMEX futures contract positioning being manipulation is coming to the main stream media and that could change things dramatically (for the good). I have no experience (does anyone?) in the financial world of an upstart Internet community shaping what main stream media may do next, but it will be interesting to observe in precious metals.

One final observation and something I have been thinking about a lot for years that has come to mind again in light of this discussion. Having studied silver and the markets directly related to it very closely for decades, there are some things I just Â?knowÂ? and I say that in humility, not as a know it all. Let's face it Â? someone who lives, breathes and studies one specific issue and gets professionally compensated for sharing his or her thoughts most likely knows more about that issue than does someone who merely dabbles in that same issue from time to time. I'm not talking just about me and silver, I'm speaking of anyone who devotes all their time to an issue, any issue, compared to someone who follows so many different issues that there is no specialization in any one issue.

My point is this. I have read non-stop negative commentary on gold, mostly in the main stream media, by more people that I never heard from before and none of which even mention the main driver of price, COMEX positioning. Therefore, I have come to conclude that when it comes to gold (and silver), there is absolutely no substance or relevance to main stream media coverage (other than as a contra-indicator). But here's my real point Â? is it this way in everything else as well? What about the endless commentary in the main stream media on stocks, bonds and every other topic or issue? If the commentary is so off the mark in gold and silver as I know to be, doesn't that suggest it's probably off the mark in everything else as well? What kind of world do we live in and who to believe?

The turnover or physical movement of metal brought into or taken out from the COMEX-approved silver warehouses remained fairly high this week as close to 4 million oz were so moved and total inventories fell again by 1.1 million oz to 177.8 million oz. Earlier in the week, there was another 0.6 million oz movement into the JPMorgan warehouse and I suspect that another 4 million oz may soon be deposited in keeping with JPM's pattern of acquisition of silver via COMEX futures contract deliveries and subsequent movement of that metal into their own COMEX warehouse. There was a bit of a flurry in COMEX gold warehouse movement this week, but still no commodity comes close to COMEX silver warehouse movement. And I still think that suggests tightness.

There has been no liquidation or reduction in the metal holdings of the big silver ETF, SLV, this week, despite the series of new price lows. Over the past month, metal holdings in SLV have actually increased by 3.5 million oz, thus preserving the counterintuitive deposit/withdrawal pattern made obvious over the past few years. Combined with the silver I believe JPMorgan has acquired over this time, it would appear that while the price has been horrid, silver appears to be very strongly held. Silver metal holdings in SLV have basically flat-lined over the past few years and are still within 10% of the peak in holdings in 2011. Just to be clear, I don't believe JPM holds much of the metal in SLV; it holds metal apart from SLV holdings (but JPM got most of its silver from the SLV over time).

In contrast, there have been sizable withdrawals in the big gold ETF, GLD, on the order of 1 million oz over the past month to the lowest levels of gold held in the trust since 2008. From the peak in holdings since the beginning of 2013, gold holdings have fallen close to 22 million oz, or 50%, in GLD. While the (lack of) metal withdrawals from the SLV is counterintuitive considering the price decline, the gold metal withdrawals in GLD look to me to be in keeping with typical investor behavior. I know that I just labeled the outburst of main stream media negative gold commentary as lacking substance, but that doesn't mean it is without effect.

Both SLV and GLD are investor friendly means of holding each metal because, for one thing, the securities make it easy to buy metal Â? perhaps too easy. (I'll save for another day the merits or lack thereof of holding such shares, but I still hold SLV). Because it's so easy to hold shares, I believe a number of GLD holders, who weren't strongly convinced or aware of the COMEX price setting, have succumbed to the negative gold commentary and in conjunction with the move to 5 year price lows have liquidated holdings. I believe this is bullish for the price of gold, as it is generally constructive for price when weaker hands are liquidated.

But if investors are liquidating holdings in GLD, they are certainly not liquidating physical holdings of Gold Eagles, according to the latest US Mint statistics. A very significant 143,000 ounces of Gold Eagles have been sold so far in July, the highest total since April 2013. Considering that the Mint may have adjusted its Gold Eagle production capacity downward to reflect lower sales over the past few years, I suppose it's possible for the Mint to have to ration sales if current demand is maintained. And since I'm not getting feedback of strong retail demand for gold (in contrast to strong retail silver demand), I'm starting to think a big buyer may account for the recent surge in demand for Gold Eagles. A supporting indicator is not as big an increase in the demand for fractional Gold Eagles favored by retail buyers, as opposed to higher proportional demand for the full ounce coins.

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

It has been reported that the Mint will announce sales of Silver Eagles on Monday, for the first time in three weeks. With no sales reported due to the sellout earlier in the month, no comparison with Gold Eagles can be made at this point. I did get a question from a long term subscriber asking why the Mint doesn't just offer whatever Silver Eagles it can produce on a daily basis, rather than hold coins off the market until it builds up a bigger accumulated inventory. It's a good question.

I don't speak for the Mint, and to my mind it is engaging in a deliberate attempt to cool off demand and is something the Mint has done (mostly successfully) on many prior occasions. By intentionally withholding Silver Eagles until it builds up a bigger inventory, the Mint forces buyers to seek out other sources of supply while sales are suspended or simply to go without buying silver. The Mint hopes, therefore, that demand will be diverted or buyers may change their minds in time to the extent that it will meet demand eventually as it stalls and withholds coins. I have mixed feelings on my premise.

On one hand, I have and can see the attempt as effective and Â?workingÂ? in the Mint's primary mission of ending the rationing of Silver Eagles by temporarily and artificially reducing demand. But on the other hand, it seems a dubious effort to end run the legal requirement of the Mint to produce enough Silver Eagles to meet demand and the Mint should stop resorting to such tricks and simply increase production. My premise aside, it is simply amazing how strong have been sales of Silver Eagles over the past 4 years that the US Mint has struggled to keep up with demand (thanks largely to the swell folks at JPMorgan) tells us a lot about how much silver may be available to buy at any one time.

It would be an understatement to say I was relieved to read the latest Commitments of Traders (COT) Report, in a way that may surprise you. Sure, I was happy to see that the changes dovetailed closely to what I was expecting and to spare myself the public embarrassment of missing by a wide margin, but I was mostly relieved for a different reason. Even though I came very close in my published expectations, I confess to having a private fear, bordering on dread that the report would come out much differently. Adding to my dread was that I received a number of emails from subscribers asking what if the new report featured heavy managed money short covering and profit taking instead of my expectations of managed money selling.

This is an issue that I may have to face someday, so let me face it today. The core of my COT analysis is that managed money (technical funds) buy and drive prices higher or sell and drive prices lower. A big part of the premise is that commercial traders orchestrate or trick the technical funds into buying and selling because the commercials control the pricing mechanism (through HFT, spoofing and the like) and the commercials' intent is to buy what the technical funds can be persuaded to sell. Sunday evening's take down in gold was just the most recent occasion to see the premise on full display. Therefore, it would be expected that the current COT report would feature managed money selling and commercial buying, just as it did.

But what if managed money traders had bought significant quantities of gold and silver contracts on this latest price takedown reaping big profits and the commercials were big sellers and big losers? It did happen in silver last fall, due to some very extenuating circumstances, but what if that became a regular pattern, namely, of having the managed money technical funds beating the commercials on a consistent basis? As much as it would pain me, if the technical funds took to beating the commercials on a regular basis, my basic premise would go down the drain.

I'm not talking about an unusual reporting week here and there, but a steady pattern of the technical funds taking big profits at the expense of the commercials would invalidate the premise as I see it. I think it important to spell out what would make a premise correct or not and having just done so, I am particularly relieved that this week nothing invalidated the premise. But reading all the negative commentary and watching prices melt on a daily basis, I suppose it is natural to question one's convictions and I'd be lying if I told you that I did not so question myself this week. Clearly, I'm not happy to see gold and silver prices, particularly the mining company shares, drop so much; but understanding why they dropped has never been more evident Â? the commercials succeeded in forcing more managed money selling.

In COMEX gold futures, the total commercial net short position declined by a very hefty 26,900 contracts to 21,600 contracts the lowest (most bullish) position in years. (I had guessed 20,000 contracts, so was bit under for commercial buying; but managed money selling was under 12,500 contracts, so I was over on that basis. Averaged together, 20,000 was darn close.) Once again, I have to forego commercial category analysis since managed money traders are now in the ranks of the big 8 shorts. Categories aside, the ultra-low commercial net short position is ultra-bullish for gold prices going forward.

In selling 12,400 gold contracts, comprised of 2116 contracts of long liquidation and 10,317 contracts of new short sales, the managed money traders set new records on both a gross and net short basis (as was noted in the Zero Hedge article above). The long side of managed money is down to just over 106,000 contracts and the short side is up to a record of nearly 120,000 contracts. Since the Tuesday cutoff, it would appear commercials bought and managed money traders sold even more.

At first, I was surprised that the managed money traders sold only 12,400 net gold contracts, while the commercials bought nearly 27,000 contracts, but as it turned out the two categories that made up most of the difference were the type I would like to see sell. Smaller non-reportable traders added 6500 new shorts and traders in the other large trader speculative category also added close to 6000 new shorts. After the managed money traders, the two next best traders that a bull likes to see go short are small traders and other large speculators, particularly on dramatic new price lows. All three categories, managed money, small traders and other reporting traders are not considered to be strong short holders and historically all will rush to buyback short positions on a price increase. They are all rocket fuel to the upside when gold prices turn, just at slightly different octane ratings.

In COMEX silver futures, the commercials reduced their total net short position by 4400 contracts to 11,200 contracts, one of the lowest (most bullish) readings in COMEX history. (I had guessed 5000+ contracts, so was bit over in the commercial count; but managed money traders sold more than 5700 contracts, so I was under by a bit and the blended number was spot on). Since there is no mathematical doubt that some managed money traders reside among the largest 4 and 8 traders on the short side, my commercial category calculation is still not operative (that doesn't matter much at this point).

Managed money traders sold and liquidated 2201 long contracts and added 3552 new short contracts. While falling just shy of the all-time record gross short position of two weeks ago, this week's reading of 55,303 short contracts is the second largest on record. On a net basis, however, the managed money short position is an historical record. (Managed money traders in gold set records on both a gross and net short basis).

The liquidation of managed money longs brought the gross long side to 40,552 contracts, right up against my often mentioned 40,000 contract core non-technical fund long position. More recently, I had speculated this core long position had crept up towards 44,000 to 45,000 contracts, but that speculation wasn't accurate in hindsight. I still believe that we shouldn't dip much below 40,000 contracts in managed money longs and if I'm correct, that suggests limited additional long liquidation from here on lower prices.

If the new reporting week were closed out as of yesterday, there would most likely be further improvements in the COT market structure for gold and silver, but I would think dramatic improvements from here would be limited by the capacity of the technical funds to add to shorts. By the way, there were dramatic improvements or increases in managed money selling in copper and crude oil and a lesser improvement in platinum.

More than ever, the prime driving force to the current commodity price downdraft is futures positioning and not some approaching end of the world as we know it. The good news associated with this is multifaceted. We will see a dramatic upturn in prices mos

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