July 9, 2016 – Weekly Review

Weekly Review

As a result of a dramatic upside reversal on Friday, the price of gold and silver finished higher for the sixth week in a row, a fairly rare occurrence over the years; with each establishing weekly closing highs not seen in a couple of years. For the week, gold finished $23 (1.7%) higher, while silver ended up by 50 cents (2.5%).

Due to silver's slight relative outperformance, the silver/gold price ratio tightened in by half a point to under 67.5 to 1. This is also close to a two year extreme in the ratio, indicating silver is less undervalued relative to gold at any time in nearly two years. The short term direction is anyone's guess, but longer term, silver still looks deeply undervalued relative to gold, at least to me.

Volume was extremely heavy on Friday, as prices were first sent sharply lower on the release of the monthly employment report (or a planned HFT computer takedown), but reversed over the remainder of the day. From its low, gold recovered by more than $30 and silver by more than a dollar. I don't like to read too much into any one day's price action, but yesterday's trade was in keeping with overall recent trading Â? higher prices despite fairly obvious attempts by COMEX commercial shorts to rig a selloff.

I say this based upon the ongoing flow of data from the COT and Bank Participation Report, where new record extremes were set in both commercial short selling and also concentrated short selling in COMEX gold and silver. Considering that the record commercial short positions have resulted in both unprecedented unrealized losses and a continued extreme exposure to further loss, the strongest proponents for lower prices would be those most short, namely, the 8 largest short traders in COMEX silver and gold.

I can't know that these big shorts are desperate or how desperate they might be, but on Wednesday I noted that the CME would likely increase margins on silver futures contracts at the first sign of a price reversal and less than 24 hours later and amid signs that prices were moving lower, the exchange instituted its first increase in silver margins. The CME has a history of resorting to margin increases designed to benefit the shorts by only increasing margins after and as prices reverse from an upside move. Like most organizations, both legitimate and criminal, the CME looks to aid its most important constituents and no members are more important to it than the biggest commercial traders.

I also can't know if actions taken by the exchange will prove successful, but I am fairly certain the commercials will do everything they can to cause prices to fall. Try to come up with a legitimate bear case that doesn't include and revolve around the market structure on the COMEX. If you find one, let me know, because I've been looking for years to no avail. I'll get into the most recent positioning changes in a moment, after the usual weekly format.

The turnover or physical movement of metal brought into and taken out from the COMEX-approved silver warehouses came to just over 4 million oz this week, as total silver inventories fell 0.7 million oz to 150.4 million oz. While this was the lowest movement in five weeks, it was a four day work week and a million oz a day is nothing to scoff at. There was a near 0.3 million oz withdrawal at the JPM warehouse, but my biggest take away is that it appears that JPM is caught up with moving all the silver it took delivery of in the May futures delivery period into its own COMEX warehouse.

July is traditionally a big delivery month for silver on the COMEX, but so far this month, JPMorgan has taken a bit of a backseat in that it doesn't appear to be pressing for the full 1500 contracts (7.5 million oz) allowed to any one stopper, as it has over the past year and a half. More than a week into the delivery process, JPM has taken 264 of the 1110 total silver deliveries issued, or Â?onlyÂ? 24% of the total so far. (HSBC is the month to date leading silver stopper, haven taken 558 contracts).

http://www.cmegroup.com/delivery_reports/MetalsIssuesAndStopsYTDReport.pdf

JPMorgan has been the leading and almost exclusive stopper of COMEX silver deliveries since March 2015 (in its own house or proprietary trading account), so the change in pattern this month is noticeable. With around 1300 contracts remaining open in the July contract, it still looks like JPM will end up with 600 silver contracts by month's end, but new contracts can and have been added since the first delivery day, so this could change. My sense is that JPMorgan knows the physical silver market is tight and has chosen not to test just how tight it has become.

Over in the COMEX July gold contract, a non-traditional delivery month, after taking more than 6700 contracts (670,000 oz) in the June contract for delivery in its own name, JPMorgan has taken no gold deliveries this month in its own name. However, a customer(s) of JPM, having taken over 4000 contracts in June, has also taken close to 2500 gold contracts so far this month. (HSBC remains the big gold issuer this month, just as it was in June).

There are still around 1200 contracts open in the July gold futures contract, so it looks like JPM's customer(s) may end up with the maximum 3000 contracts allowed. Of course, last month both JPM and its customer took much more than the 3000 contracts allowed, but apparently, limits apply only to the little people or those not affiliated with JPMorgan. Finally, it is too soon to discern any pattern, but 131,000 oz (1310 contracts) were deposited into the JPMorgan COMEX gold warehouse this week, perhaps suggesting more to come, ala silver, in light of how much gold JPM took delivery on in June.

In addition to more than one million oz of gold coming into the big gold ETF, GLD, this week, nearly 8 million oz of silver were deposited in the big silver ETF, SLV, the most in quite some time. This is as it should be, given the obvious net buying recently in both GLD and SLV. I'm still puzzled by the apparent ease with which physical gold has been made available to GLD and for COMEX deliveries and will say the same thing should many millions of additional ounces of silver be deposited into SLV with equally apparent ease. So far, there does seem to be more of a delay in depositing silver than gold that is in keeping with my feelings of greater physical tightness in silver than in gold. But in both gold and silver, I have a sense that physical metal is being deposited faster than usual in keeping with the only remedy for arresting a developing bank run, namely, give everyone asking for money (or metal) as much as they want in the hopes of preventing a full blown panic from developing.

Sales of Silver Eagles from the US Mint ended June punk and that has continued into July. Ironically, reports from the retail dealer front indicate that the holiday shortened week was among the strongest in months, no doubt prompted by world news and price action. As I indicated on Wednesday, what sets the price of silver is metal in the form of 1000 oz bars, but public retail demand for other forms of silver help clarify overall investment demand. Weak reported sales from the US Mint despite reports of resurgent retail demand only confirm, in my opinion, the role of JPMorgan in buying Silver Eagles. Just like the case with the bank not pressing for deliveries this month on the COMEX, JPM stepping aside from buying Silver Eagles may reflect just how tight silver has become.

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

Onto the changes in this week's Commitments of Traders (COT) Report, where another week witnessed new record extremes in commercial shorting and technical fund buying. I intentionally did not predict what the changes this week might be, because last week a massive increase in total open interest in COMEX gold turned out to feature a massive increase in spread positions, which for all intents, are market neutral.

In the previous reporting week, an increase of more than 40,000 contracts in total gold open interest resulted in Â?onlyÂ? a 14,000 contract increase in commercial shorting, causing me to overestimate the commercial increase. Not wishing to do that again, I held off on estimating this week because of the spreading anomaly. As it turned out, this happened again, as the 40,000 contract increase in this reporting week's gold open interest resulted in a 14,000 net increase in commercial shorting due to another massive increase in spreading. Why so many gold spreads are being established is a mystery for me, but I can make no connection with prospective price direction.

In COMEX gold futures, the commercials increased their total net short position by 13,900 contracts to yet another record of 340,200 contracts (34 million oz). Somewhat interestingly, this is the third week in a row where the commercial short position increased by around 14,000 contracts. I have and would characterize the new record gold short position (for silver as well) as being bearish, based upon historical patterns and the mechanics of COMEX price setting; but it goes without saying that should the commercials fail to turn prices lower and set off technical fund selling, the Â?bearishÂ? market structure could turn into the most bullish event ever.

By commercial category, the 4 largest commercial shorts added 7100 new short contracts, the big 5 thru 8 shorts added 3700 new shorts and the raptors (the smaller commercials apart for the big 8) added 3100 new short contracts. In addition to the total commercial net short position being at a record, the concentrated net short position of the four largest commercial shorts hit a new record of 199,809 contracts while the concentrated short position of the 8 largest gold shorts is now at a record 292,531 contracts.

Four traders are net short 20 million ounces of gold, or an average of 5 million ounces apiece and 8 traders hold 29.2 million oz, or an average of 3.6 million gold ounces each. These eight traders hold 86% of the record amount of gold held net short by commercials on the COMEX. I would ask you to reflect on this for a moment.

For some reason (maybe because it must be calculated by hand), there is much discussion on the record large short positions in COMEX gold and silver, but hardly any discussion about how so few traders hold the short position. I must have used the term Â?concentratedÂ? a gazillion times on these pages, but clearly a gazillion is not enough. If a record short position was held by hundreds of traders, all acting independently from each other, it wouldn't matter all that much how large the short position was. In a very real sense, the more traders, the merrier.

If any market position, short or long, was held by many traders, no matter how large the overall position may be, manipulation would be impossible and the likelihood of a market Â?accidentÂ? would be remote. In free markets, the greater the number of participants, the more free those markets would be considered. There can never be too many traders in any market, just too few.

Should a large market position be held by just a few traders, the concept of free market is turned on its head. A small number of traders (say 4 or 8) holding a large position is markedly different than the same large position being held by many different traders. This is the reason the CFTC monitors and publishes concentration data in the first place, despite so few picking up on it. The problem is that the CFTC refuses to act on concentration even after establishing it exists in spades in COMEX gold and, particularly in silver.

Aside from manipulation being defined as prices being artificially controlled by a small number of players, any market so controlled creates the possibility that things could suddenly come undone should any of the few who are manipulating prices run into financial difficulty. Hardly impossible, this is the story of Bear Stearns, AIG and Lehman Brothers that is being replayed in COMEX gold and silver. The sooner the discussion turns to the concentrated nature of the gold and silver short position, the better I believe it will be because that's the real crime and nub of the issue.

Back to the gold COTs, the managed money traders accounted for most of the buying as they bought more than 12,000 contracts, including adding 14,175 new longs while shorting just over 2000 contracts. This is yet another new gross and net long position by the managed money traders.

In COMEX silver futures, the commercials increased their total net short position by 3600 contracts to 98,800 contracts, either the largest ever or for as long as it matters on a practical basis. By commercial category, the 4 largest shorts added 1200 new shorts, while the raptors sold 3200 contracts, completely eliminating their net long position and ending up 700 contracts net short. Balancing out, the big 5 thru 8 bought back 800 short contracts. Despite that buyback, the concentrated net short position of the 8 largest traders set a new record of 98,065 contracts or 490 million oz, while the four largest traders set a new record for concentration with 68,476 contracts (342 million oz) held net short.

As a result of the release of the new monthly Bank Participation Report, I must increase my estimate of what JPMorgan holds short to 28,000 to 30,000 contracts and perhaps even more than that, up from near the 25,000 contract mark. It's not as if JPM increased its silver short position by that much in the past week, it's more a case that I can only recalibrate when the monthly BPR is released. At first I was disappointed as that was not in conformity with my double cross premise, but a colleague pointed out that JPMorgan would likely try to cover its tracks any way it could. He pointed out JPM could offset the short quantities added in other markets with ease.

On the buy side in silver, the managed money traders bought 90% of what the commercials sold, in buying 3323 contracts, including the purchase of 2489 new longs and the short covering of 834 contracts. As was the case in gold, the managed money traders set new records for long positions, both on a net and gross basis. Still, the central issue is the matter of concentration on the short side.

That only 8 traders hold 490 million ounces of silver net short and the CFTC is openly reporting this is mindboggling. This is more than 50% of either annual world production or the entire visible supply of 1000 oz bars in the world. But it's much more than that. If this short position was held by 8000 or 800 or even 80 traders, I would have trouble complaining about it. But 8 is too few, as is 4.

Please remember, I didn't choose either the number 4 or 8 as the threshold for concern Â? the CFTC did that on its own in every commodity it reports on. And when you review every other commodity that the agency reports on and take the concentration data and apply it to all the markets, guess what? In terms of real world production and inventory levels, COMEX silver shows up as the most concentrated on the short side with COMEX gold now in second place. Isn't it natural to then ask why this is so? Why are there such concentrated short positions in COMEX silver and gold and what does this mean?

It means, at a minimum, that if the concentrated short positions didn't exist, silver and gold prices would be much higher. Not would be higher, must be higher because in the absence of the concentrated short selling by a few, that selling would have to be replaced by others willing to go short at current price levels. But if there were many other traders willing to go short at current levels, they would have already gone short and the concentrated short positions wouldn't exist. The simple fact is that silver and gold prices aren't high enough to attract enough traders away from the 8 crooked traders already short.

Worse, the 8 concentrated short sellers in COMEX silver and gold are largely, if not exclusively banks and financial institutions, most in the too big to fail category. What this means is that systemically important financial institutions, many backed by the US Government if they were to get into trouble, are the big short holders in COMEX gold and silver and are directly responsible for manipulating prices. It's almost too crazy to conceive Â? the federal regulator responsible for guarding against manipulation, the CFTC, is openly reporting data that proves the manipulation and then looks the other way. Should things go wrong (and continue along the current path) the US Government will have no choice but to bail out the big short sellers. (All except JPMorgan, which has bailed itself out already by its massive accumulation of physical silver).

But things may be going wrong already and might be at the point of no return. The scorecard of the money game I have been featuring lately would indicate great financial stress as a result of the gold and silver rallies over the past six weeks. I don't sense much additional damage to the shorts over the past two days, but neither have the unrealized financial losses diminished in any way. Net-net for the year, the commercials short in COMEX gold and silver are in the hole for $2.5 billion and those losses, like the position itself, is largely concentrated among 8 traders. Every $10 move in gold higher adds $340 in additional losses and every dollar in silver higher adds $350 million (removing JPM's 150 million oz short position).

Price moves to the downside will be to the crooked commercials' advantage and the sheer numbers involved provide all the motivation the commercials need to rig prices lower. It's no secret the commercials will rig prices lower if they can, the operate question revolves around their ability to do so. One thing I am certain of is if the commercials' current predicament and vulnerability were to become more known in the macro hedge fund community (away from the pure technical fund community), more hedge funds would take it to the concentrated commercial shorts. Even if that awareness doesn't develop, should enough continued buying come into gold and silver ETFs that would probably be sufficient to end the COMEX scam. Time will tell.

Ted Butler

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Silver – $20.30 (50 day moving average – $17.42)

Gold – $1366 (50 day moving average – $1279)

Date Created
2016/07/09