

June 18, 2014 – Big Money

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A story in the Financial Times (London) over the weekend regarding central bank and other public institutional investments set off a round of commentary and discussion. The FT article was based upon findings by a research and advisory group (OMFIF) in a press release <http://omfif.createsend1.com/t/ViewEmail/j/AD679A12EEB1FB26>

The advisory group defined public investors as central banks, public pension plans and sovereign wealth funds, amounting to some 400 such institutions in 162 countries. It found that total investment holdings by these global public investors approximated \$29 trillion; with central banks holding \$13.2 trillion (including gold holdings), \$9.4 trillion in public pension funds and \$6.5 trillion in sovereign wealth funds. Because interest rates had fallen to such low levels, the study found that public investors as a whole had put as much as \$1 trillion into the world's equity markets in recent years (although the press release didn't specify total stock market holdings).

Since central banks are said to hold approximately one billion ounces of gold bullion, worth some \$1.3 trillion, the gold holdings of central banks are roughly 10% of their total investment holdings. This percentage is remarkably close to the recommended portfolio allocation of many gold proponents, although most central bank gold holdings date from many decades and even centuries ago. The press release didn't specify the gold holdings of public pension or sovereign wealth funds, but it is thought those holdings are less in percentage terms than that of central banks.

Because the percentage of silver holdings is effectively zero among the world's public investors, the growing potential buying power is more bullish for silver than for any other asset, including gold. Not only is it not possible for public investors to sell and flood the market with physical silver bullion (since they don't own any), any investment in silver would have a profound impact on the price considering how little silver bullion exists (\$25 billion worth) compared to total public investment assets. One-tenth of 1% (0.1%) of \$29 trillion is worth more than all the world's silver bullion at current prices. With the average holding of the world's 400 public investors sitting at \$725 billion each, any one of these public investors could cause the price of silver to multiply.

But why stop at the world's public institutional investors, as they do not represent the bulk of world investment buying power. To get a better handle on potential investment buying power, please consider that total personal financial wealth in the world runs north of \$200 trillion, seven times public institutional holdings. Primarily split between equities, real estate and interest bearing instruments, total personal wealth also includes gold holdings of almost \$6 trillion (ex-official holdings) or 3% of total world personal financial wealth.

There is no doubt that should the world's investors (public and/or private) divert a larger percentage of total wealth towards gold, both the price and total value would rise accordingly. After all, this is the basic investment premise for gold. And while the same could be said about the investment demand component of silver, until you sit down and ponder the actual numbers, you can't fully appreciate the potential impact on silver prices that would result on the smallest diversion of total world personal wealth.

Since most total silver production (mine + recycling) is consumed industrially or in total fabrication demand, the amount of newly produced metal available for investment demand is relatively small. Of total annual production of roughly one billion ounces, only about 10% of that, or 100 million oz, is available to world investors annually. By coincidence and because little gold is used industrially (10%), there is also the same amount of newly produced gold available to world investors annually, or 100 million oz. The big difference is in the dollar amounts of the same 100 million oz at current prices; for silver it comes to \$2 billion annually, for gold it comes to \$130 billion each year.

If there is one key to unlocking the true essence of silver supply and demand, it is in appreciating that only 10% of the total new supply is available for investment after all fabrication demand is accounted for. While it's an old story — silver's physical and chemical properties make it an indispensable industrial material — it is still an underappreciated story. A billion oz of annual production only creates 100 million oz of new investment silver (in 1000 oz bullion bars). Yet, it is clearly the 10% investment demand component that dictates the price.

With \$200 trillion in total world personal financial wealth (plus \$29 trillion in public institutions), the \$2 billion of newly produced silver available for investment annually represents one one-thousandth of a percent (0.001%) of total wealth. Moreover, since total financial wealth is far from evenly distributed, even that becomes a potential plus in silver (and gold) in that a relative handful of world investors could impact prices by themselves. In other words, so little money is needed to absorb all newly produced silver that great numbers of investors would not be needed to jolt prices upward. Besides, there is so little actual silver available, there is no way large numbers of silver investors could be accommodated.

Apart from the small percentage of newly produced silver, the only other metal potentially available to investors is the existing world inventory of 1000 oz bars. Total visible and documented silver bullion inventories are less than 900 million oz, but I suggest undocumented inventories may increase total inventories to 1.3 billion oz. Of course, I could be wrong (how do you document that which isn't documented?) and there may be less than one billion oz of silver bullion in the world.

Still, in dollar terms, there is only \$20 to \$25 billion worth of silver bullion in the world or one one-hundredth of one percent (0.01%) of the \$200 trillion of total personal financial wealth. By comparison, total world gold holdings of 5.5 billion oz are worth more than \$7 trillion or 300 times the value of total silver bullion. Of course, all the world's silver bullion is owned by a wide variety of investors, so it is somewhat presumptuous to call it available. Only the actual owners will determine at what price the silver is truly available. All the silver bullion in the world is very much different than all the available silver bullion in the world. One thing much more certain is that \$200 trillion worth of world personal wealth exists and if the smallest fraction of one percent of that wealth tries to buy the metal, the price lid will be blown off.

In fact, when comparing how much buying power could suddenly shift to silver versus the incredibly small quantity of metal available for investment, I wouldn't blame you if you questioned the numbers I have presented. That's because the numbers don't mesh with silver prices over the past three years. What I have presented should have resulted in much higher silver prices than actually experienced. So, by all means, please check my numbers and let me hear from you should you take issue with any of them.

If you find my presentation of the numbers reasonably accurate, an explanation for the disparity between data and price should then be demanded. The only explanation possible is the ongoing price manipulation on the COMEX, where a massive short position held by 8 commercial traders has depressed the price. With more than 300 million oz of silver held short in concentrated form, 8 traders on the COMEX have sold short the equivalent of all the metal from new production available for world investment for the next three years. How could that not depress the price?

Considering how many new observers are tuning into the COMEX silver manipulation, both as an explanation for the dirt cheap silver price and for the investment bargain the manipulation has created, it is hard for me to believe the manipulation can continue indefinitely. Eight concentrated short traders will be increasingly exposed to scrutiny for their crooked COMEX dealings and increasingly aligned against the \$200 trillion of personal wealth in the world that is growing.

I know these 8 crooked COMEX shorts have set the price of silver up until now, but any move to silver by the world's investors will likely be away from the COMEX and towards physical metal (including world silver ETFs). As and when world investors buy up the 100 million oz of new silver available annually along with whatever amount of world inventories existing silver owners are willing to part with, the stage will be set for a physical shortage where investors and silver users will compete for available metal. That will be the blow-off phase when silver investors will be dancing in the street.

Updating since Saturday's review, one surprise was the withdrawal yesterday of nearly 2 million oz from the big silver ETF, SLV. Based upon trading volume and the upturn in silver prices last week, I had expected a deposit of as much as 2 million oz instead; therefore, an explanation is in order. Since net-selling in SLV is quite unlikely on advancing prices, the most plausible explanation for the withdrawal is that shares were converted to metal and the metal was shipped out of the trust to somewhere it was more needed.

Confirming what can only be called tightness in the wholesale physical silver trade has been the continued heavy turnover in the COMEX-approved silver warehouses this week. For the first two days of the week, close to 2.5 million oz have moved in and out from the warehouses. The continued rapid movement of physical metal into and out from the COMEX silver warehouses is aligned with the surprising withdrawal from SLV as pointing towards physical silver tightness.

I'm writing this as the market awaits the FMOC announcement. This has absolutely no legitimate connection to the price of silver or gold, other than to serve as a handy cover story for whatever way the commercials choose to rile the market. So, apart from the shortest of short term price movement, the focus should still be on the market structure. There was likely some increase in the headline total commercial net short position to be reported Friday, but most of the increase appears to have occurred last Thursday.

Since then, COMEX trading volume and price movement have been contained and with little volume and price movement, the structure can't change much. In this case, since the existing market structure was strongly bullish, particularly in silver, no big change is good news. With an extreme short position still in place by the technical funds, there is the near certainty of an eventual upside resolution, regardless of short term price action. I suppose more tech fund shorts could be lured into the market on lower prices first, but the structure will only be resolved on the inevitable higher prices to come.

After a year where price lows in silver have been sub-\$19 on a number of occasions, it appears to many that silver will never rally as it had prior to the price highs of three years ago. Yet, everything is in place for a sharp rally, perhaps even developing into the long-awaited moonshot. There is surely more world investment buying power today than ever in history and less silver available to satisfy potential investment demand. Throw in an increasingly obvious price manipulation and the technical funds so overloaded on the short side of the boat that any shift may capsize the silver boat and send prices soaring.

Ted Butler

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Silver – \$19.80

Gold – \$1273

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