June 21, 2014 – Weekly Review

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Due to sharp gains on Thursday, gold and silver experienced their best week in months, with gold ending $39 (3.0%) higher and silver up by $1.20 (6.1%). As a result of silver's relative outperformance, the silver/gold price ratio tightened in by nearly two full points to 63 to 1. This the tightest the ratio has been in almost 4 months, but still within the broad trading range of the past year and longer. But it may be a mistake to read too much into silver's relative outperformance, as I detected no discernable preference for silver over gold this week and the price performance, both relative and absolute, was dictated by something quite specific and singular.

The reason for this week's (Thursday's) price blast was so well documented beforehand and so fully expected that I was more taken back by the news accounts (mostly mainstream media) that were clueless about the real cause of the sudden move up. Of course, I am referring to the massive technical fund buying (mostly short covering) that drove gold and silver prices higher on the COMEX. At least for this week, nothing else mattered for the price of gold and silver.

While I know that I have been almost maniacal in my attention to the extreme level of technical fund shorts in COMEX silver (and gold), both as the explanation for why silver price action was so dismal this year and why the eventual short covering would prove explosive to price; I was far from alone. In fact, the number of Internet commentaries that spoke of the record technical fund short position in COMEX silver and what would inevitably occur once these shorts were bought back and covered were greater than ever before. I think that's a testament to the growing importance of the market structure on the COMEX, as is revealed in the COT reports.

Despite the confusion on the part of many who only look at gold and silver from a distance as to what the sudden price jump was all about, the truth is that I was more surprised that silver prices jumped as little as they did considering the force and urgency of the technical fund short covering. The question was never if the technical funds would buy in unison with Â?at the marketÂ? buy orders; the question was always how forceful would the commercials (raptors and big 8 shorts) be in selling to those technical fund urgent buy orders. The answer so far is that the raptors, at least, have been quite forceful in their selling of long positions. More on that in a moment.

After a couple of weeks of Â?below averageÂ? turnover or movement of actual metal into and out from the COMEX-approved silver warehouses, the movement jumped sharply this week to nearly 5.9 million oz, as total COMEX silver inventories fell 1.7 million oz to 174.5 million oz. Please don't confuse this actual physical silver movement with the trading of futures contracts. Yes, the trading and positioning of futures contracts is enormous and does set the price of silver, while the massive turnover of actual metal in the COMEX warehouses has had little to do with determining the price of silver to this point.

But there may come a day when the physical tightness indicated by continued COMEX warehouse movement morphs into a full-blown silver shortage. At least that's my take. More than 100 million oz of actual silver in 1000 oz bar form have been moved into and out from the COMEX silver warehouses this year to date, while total inventories have remained unchanged. This is very unusual and, as far as I know, has never occurred in any other commodity. Unusual events cry out for explanation and the only plausible (or possible) explanation for the unusual movement in the COMEX silver warehouses appears to be such tight conditions in the wholesale physical market so as to require constant deposits of metal to satisfy the constant demands for physical material.

This week offered supporting evidence of physical silver tightness in developments in the big silver ETF, SLV. For the past couple of weeks and particularly this week, the price of silver has risen amid heavy trading activity, both in COMEX futures trading and in the volume of shares traded in SLV. On Thursday and Friday, the trading volume in SLV was the highest two day volume on an upside move since last September. Whenever there is a great surge in trading volume in SLV to the upside in price, it is axiomatic that net buying of shares occurred. New net buying requires that new metal be deposited into the trust to back the new shares created. The only way that new deposits of silver can be avoided is if the sellers of SLV shares go short the shares in lieu of depositing metal as is required by the prospectus.

Based upon price action and trading volume in SLV over the past two weeks thru yesterday, some 7 million oz are now Â?owedÂ? to the trust. Instead of metal deposits, SLV has experienced fairly large withdrawals, further suggesting tightness in wholesale physical silver. Even if SLV receives silver metal deposits in the days ahead, the delay in making those deposits supports the tightness premise. If we do experience an increase in the short position in the short report due in a few weeks (not necessarily in the report due next week), that will also suggest that metal wasn't available for deposit due to tight silver supply circumstances.

If we do witness a sharp growth in the short position of SLV, I'm prepared to take the matter up again with BlackRock (the trust's sponsor) and their very aggressive lawyers. The bottom line is that the lack of deposits/delay in SLV fully supports the COMEX silver warehouse turnover as an indicator of extreme tightness in physical silver. As much as I study the COTs, as and when a pronounced physical shortage of silver appears, I'm prepared to disregard the COTs as physical will trump paper. Again, both the COMEX warehouse turnover and the deposit story in SLV are specific and unique to silver and not any other commodity, including gold.

The changes in this week's Commitments of Traders Report (COT) was significant in both gold and silver and the prospective changes since the Tuesday cut-off promise to be even more significant. The headline number of the total net commercial short position increased in both gold and silver this week and undoubtedly more since the cut-off. Price action over the reporting week doesn't seem dramatic at first glance, as silver rose about 60 cents and gold by as much as $25. But the technical funds are motivated primarily by price penetrations of moving averages and gold penetrated its 20 day moving average for four days of the reporting week. Silver had penetrated the more important 50 day moving average for four days as well, explaining the aggressive technical fund short covering and raptor long liquidation.

In COMEX gold futures, the total commercial net short position expanded by 15,200 contracts to 78,300 contracts. While not a particularly large total commercial net short position, I would estimate a further increase of as many as 40,000 contracts in the three trading days since the cut-off. By commercial category, the 8 largest shorts increased their net short position by 3500 contracts as gold raptor selling of long positions accounted for the balance of commercial contracts sold. Grouped with the raptors, JPMorgan appears to have sold 3000 of its long COMEX gold futures position, reducing that long position to 34,000 contracts as of the cut-off date.

On the buy side in gold, it was exclusively a technical fund affair, as the managed money category of the disaggregated COT report indicated net buying of 15,500 contracts, including more than 13,600 contracts of short covering. With gold (and silver) prices exploding over all the important moving averages after the cut-off on massive trading volume, it's hard to imagine there could be large numbers of technical fund short contracts remaining to be covered. There is not much justification for a technical fund to be short when all the moving averages are decisively penetrated to the upside.

In COMEX silver futures, the total commercial net short position expanded by 8500 contracts, to 22,800 contracts. This was one of the largest weekly increases in history, with the two week increase of 13,200 contracts also historically significant. Based upon price and volume data since the Tuesday cutoff, I'm fairly sure we exceeded the two week increase on Thursday and Friday alone. By commercial category, it was an all raptor affair as the smaller commercial longs sold almost 11,000 long contracts for the reporting week and almost 14,000 long contracts over the past two reporting weeks. The raptors held 36.300 long silver contracts as of the cut-off, but are likely to have sold 10,000 to 15,000 more silver long contracts on Thursday and Friday.

As was the case in gold, the buy side was strictly a technical fund affair in silver as the technical funds bought more than 10,000 net contracts, including more than 9100 contracts of short covering. As was advertised well in advance, the key players in silver (and gold) were the technical funds and the raptors, the two specific categories of COMEX traders which (illegally) set the price. Without these two narrow groups of traders the price of silver never would have exploded this week; nor would it have declined this year. What I am suggesting is that this is a crazy and illegitimate way of setting silver and gold prices, as it excludes the world's real producers, consumers and investors. Why do we tolerate two specific groups of speculative traders on the COMEX determining prices for the rest of the world?

I'd be lying if I said I wasn't disappointed with how aggressive the raptors were in selling so much of their long silver position with such meager profits. I'd estimate the raptors took out or will take out maybe $1 net on the 30,000 contracts likely to have been sold, or $150 million in total. That's not chopped liver, even after being split up by as many as 30 traders, but it could have been double or triple or more than that had the raptors not been so aggressive on the sell side. Let's face it Â? the technical funds were exactly as aggressive in buying as was expected and I hope I had conveyed to you what would determine how high silver would run on technical fund buying would be determined by the degree of raptor selling aggression. Clearly, the extreme degree of raptor selling aggression must be considered disappointing.

One surprise under the hood of the silver COT report was that JPMorgan did not sell additional contracts short in the reporting week; instead buying back 2000 short contracts. In what must be termed highly unusual and not at all in keeping with past actions by JPM on silver price rallies, the bank has reduced its concentrated COMEX silver short position to 13,000 contracts. This is very close to the lowest short position held by JPMorgan since it acquired the big gold and silver short positions of Bear Stearns in early 2008. In addition to harping on the matchup between the technical funds and the raptors for determining price, I have also been insistent that the key to silver prices will be most influenced by whether the 8 big commercial shorts, led by JPM, increased their concentrated short position on the inevitable silver rally.

For this week, at least, there was no increase in the concentrated short position on a rally with aggressive technical fund buying. I'll reserve final judgment until next week's COT report is published, but I can't help but note that the short position of the four largest COMEX silver shorts is at its lowest since December and that of the 8 largest shorts since February. Since I am certain that the long term silver manipulation cannot continue to exist without the concentrated short position expanding on price rallies, I can't help but sit up and take notice when that position shrinks on price rallies. I can't say that the reduction this week in JPMorgan's short position fully removes the disappointment of the aggressive raptor selling of long positions, but similar readings next week just might.

One thing that I have noticed for some time but haven't written about is the changing composition of the 4 and 8 largest shorts in COMEX silver. Specifically, JPMorgan's share of the total concentrated short position has been shrinking and the share held by the 5 thru 8 largest traders has grown. JPMorgan now holds 13,000 contracts of COMEX silver short against 59,000 contracts held short collectively by the big 8 or, effectively, the smallest share held by JPM since acquiring Bear Stearns.

At the same time, the share held by the 5 thru 8 largest shorts in COMEX silver has grown to be the largest since I have been studying the COTs. Two years ago, the 5 thru 8 largest traders held no more than 7 or 8,000 contracts short. A year ago, the 5 thru 8's short position had grown to 10 or 11,000 contracts. In the latest COT, the 5 thru 8 largest traders are short 21,700 contracts, the highest amount in memory. The question arises Â? why has JPM's share been so reduced and the share held by the 5 thru 8 largest traders grown so dramatically?

The answer that seems inescapable to me is that my allegations of manipulation in COMEX silver, based upon the concentrated short position of JPMorgan, were so on the mark and irrefutable as to render no possible legitimate rebuttal by JPM, the CME or the CFTC. So because my allegations couldn't be explained away, the only recourse left was to reduce JPMorgan's share and increase the share held by the 7 other largest traders. As my old friend and silver mentor, Izzy Friedman repeated endlessly, if you want to figure out what criminals are likely to do, you must first think like a criminal.

Quite frankly, I have long anticipated the broadening out of the share held by the 7 other large commercial shorts and the reduction of the share held by JPMorgan because it promised to be one of the few ways the manipulation argument could be blunted. Accordingly, I am not in the least surprised by JPM's shrinking share and the increasing share of the 7 other large COMEX silver shorts. More than anything else, I believe all 8 traders as well as the CME and the CFTC are complicit in the criminal scheme to take the spotlight off JPMorgan. But I think they may have waited too long.

Because the price of silver was manipulated too low and for too long, the scheme to broaden out ownership of the concentrated short position can easily be exposed as criminal. The price of silver is so low that it is completely uneconomic for it to be legitimately hedged by any producer; that's why miner hedging is the lowest in a decade or longer. With no legitimate miner hedging possible, what could begin to explain the economic legitimacy of the massive concentrated short position in COMEX silver? In the criminal quest to take the spotlight off JPMorgan, the schemers overlooked basic economic sense.

More observers than ever see that silver prices are set on the COMEX between speculators only; with miners, users and investors excluded from the process of determining price. That's contrary to commodity law and illegitimate on its face. Throw in a concentrated short position greater than any concentrated position in any other commodity and shielding JPMorgan's role by expanding the other 7 traders' share just might fall on its face. You can be certain that I intend to press this issue aggressively.

So after the not so big price move higher on the massive technical fund buying of the past couple of weeks, what's in store? The only honest answer is I don't know. I am disappointed that so much of the rocket fuel of technical fund short covering has been burned off with only a $2 silver rally from the lows. On the other hand, I am excited by what may be strong signs of a tightening physical silver market (COMEX warehouse turnover and SLV developments) and the peculiar circumstances of JPMorgan and the concentrated short position.

I would remind you that we reached the highs of 2011 not on technical fund short covering but because of a developing physical shortage in silver, the signs of which are more similar to present conditions than not. Because we have lost the certain gimme of technical fund short covering, I'm not buying silver call options currently; but neither am I selling those calls previously acquired. Even absent the force of technical fund buying, silver could be poised for a moonshot on physical tightness considerations. I can also state unequivocally that the price rally in silver has not changed the fact that it is still the most undervalued asset in the world.

Ted Butler

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Silver – $20.85

Gold – $1315

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