

June 25, 2016 – Weekly Review

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In one of the sharpest one-day price surges in history, gold vaulted \$100 in an overnight move in reaction to the Brexit vote, retaining \$60 of the gain by yesterday's close. Due to losses every day up through Thursday, the weekly gain for gold came to \$19 (1.5%), while silver ended the week 28 cents (1.6%) higher. While the silver/gold price ratio finished unchanged at slightly above 74 to 1, it too was quite volatile intra-week.

For a change, the volatility in the silver/gold price ratio during the week came as a result of much sharper moves in gold, both down and the up, rather than in silver. Usually, sharper moves occur in silver, since it is the much smaller market, but not this week. I'm not sure what to make of it, but it was like a massive St. Bernard was jumping and yipping around a tiny Chihuahua. Usually it's the other way around. I'm inclined to think it has everything to do with massive amounts of gold positioning on the COMEX, which I'll get into in a moment.

This is the fourth week in a row that gold and silver have advanced in price, with gold closing at new two year highs and with silver not as impressive in the new high department. Since year end, gold is up close to \$260 (24.5%), with silver up nearly \$4 (29%). It seems that silver's percentage outperformance is mathematical – due strictly to how cheap it was at yearend and not because it has been leading the way higher. If you told me in January that gold would be up \$260 at this point, I would have pegged the gain in silver at more than \$4. All that said, I believe more than ever that silver's real outperformance will come in time.

If this year has been anything, it has been a testament to the growing disparity between what has been transpiring in the world of actual gold and silver metal and the world of paper trading on the COMEX. Simply put, continued signs of physical demand and tightness are evident in both gold and silver against a backdrop of historically large commercial short positions in COMEX gold and silver futures. And considering all that has transpired this week on both fronts, I don't think it's an exaggeration to say that we may be facing the ultimate test of the whole COT market structure premise. That's the premise that has largely dictated prices for decades and in which the commercials achieved mastery over the technical funds. Let me run through the actual world of metal before turning to the latest COT developments.

It was another blockbuster week for turnover or physical movement of metal brought into or taken out from the COMEX-approved silver warehouses, as nearly 8.8 million oz were moved. This is down only slightly from last week's 8.9 million oz movement, the largest movement in months. Total COMEX silver inventories rose this week by 0.8 million oz, the exact same amount they fell in the prior week, to 150.8 million oz. Total silver stocks fell to fresh three year lows intra-week, but Friday's large 1.7 million oz inflow put inventories up for the week.

The past two week's extraordinary turnover of 17.7 million oz which resulted in no change in total COMEX inventories over that time underscores the phenomenon I have been highlighting for more than 5 years, namely, the real story is in the motion, not the ocean. If silver were physically abundant in many locations, there would be no need to move it around so vigorously. That spells physical tightness to me.

Last week, I commented that JPMorgan had appeared to be actively moving the 7.5 million oz it took delivery of in the COMEX May futures contract into its own COMEX warehouse, with only 4 million oz remaining to be moved. This week, JPM moved another near 3 million silver oz into its own COMEX warehouse, so it looks like only a million oz or so are left to be moved. The most amazing thing about all this is just how open and methodical JPMorgan has been in this and other aspects of its massive accumulation of physical silver over the past five years. These guys don't appear to give a hoot about disguising the accumulation and it's a wonder more are not discussing it.

Turning to gold, the June delivery period on the COMEX is winding down, but is still one for the record books and even at this late date, some new contracts are being added for delivery. JPMorgan, both for its own account and on behalf of a client(s), has taken more than 10,600 contracts (1.06 million oz) the most ever and three and a half times more than the spot month position limit. All this, I would point out, with the bank massively net short in COMEX gold futures — more of a conflict than I could ever imagine. And I'm still mesmerized by the nearly 5400 contracts open in the non-traditional July delivery month which begins the start of its delivery period next week. I don't know what to expect — JPM demanding additional gold deliveries or for the bank to turn around and redeliver.

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

Sticking with physical gold, yesterday's massive volume (more than 35 million shares) in GLD, the big gold ETF, was the heaviest in more than three years. It appears to have resulted in yesterday's very large near 600,000 oz deposit in GLD, which follows a string of deposits. Since yearend, around 9.5 million gold ounces have come into the trust, increasing the amount of gold held in GLD by nearly 50% to 30 million oz. More than 2 million oz of gold have been deposited in GLD over the past month. These are extraordinary amounts of gold, particularly in dollar terms. The only venue where larger amounts of gold have been transacted is in COMEX futures. I understand paper is different than physical, but when the paper dealings are 3 or 4 times larger than the physical amounts, paper sets the price (until it doesn't).

One thing that strikes me, in the quest for objectivity, is where all this gold is coming from. This may sound odd, given my repetitive sermons about there being vastly greater amounts of available physical gold bullion in the world than silver bullion. But the fact is that I am quite surprised that so much physical gold has flowed into the GLD (and involved in recent COMEX deliveries) without a greater impact on price. I follow silver a bit more closely than gold, but reports over recent years have pointed to tightness in physical gold and that, I suppose, is why I'm taken back by the apparent ease with which big quantities of gold have been made available without a more pronounced impact on price.

It's not that gold prices haven't risen, as they surely have, off to the best start in 30 years. Again, if you told me at yearend that GLD holdings were about to increase by 50% and that JPMorgan would demand 3.5 times the spot month position limit in a single delivery month, I would have imagined more than a \$260 increase in price. Further, I would imagine things being somewhat out of control in the gold market. And I can't help but think that might still occur if the disparity between physical and paper grows any more extreme.

There has been no surge yet in overall deposits into SLV, the big silver ETF, along the lines of what has occurred in GLD. In fact, there have been withdrawals in SLV recently of 10 million oz, although it's closer to the truth to say that holdings in SLV have been fairly stable for five years. This is not the first time the deposit patterns between these two big ETFs have differed. Starting in 2013, holdings in GLD began a two year decline of more than 50%, from 43.5 million oz to 20.5 million oz at the end of 2015. All during that time, silver holdings in SLV were mostly unchanged in the 325 million oz range. Likewise, this year's sharp increase in gold deposits in GLD comes while holdings in SLV are around 332 million oz.

Deposit/withdrawal patterns will undoubtedly change in the future, but in looking for obvious and plausible explanations for what has transpired to date, it seems safe to conclude that metal seems to flow easier, both into and out from GLD than in SLV. I don't know that deposits in SLV couldn't possibly increase by 50% in six months, as just occurred in GLD, but the thought pattern is fascinating.

Please consider that the 9.5 million oz of gold that were deposited this year cost more than \$11 billion and that 160 million oz of silver (50% of SLV holdings) would cost less than \$3 billion, a quarter of the money spent in GLD. I guess what I'm saying is that 160 million oz of physical silver could not be purchased in six months without silver prices truly screaming higher. Incredible as it seems to me, silver has kept pace with gold despite having nowhere near the investment flows. I shudder to think of the price impact on silver as and when investment flows ramp up.

Against a backdrop of not knowing where all the physical gold and silver has or will come from, let me turn to what I believe has been the primary price driver — COMEX futures positioning and the latest Commitments of Traders (COT) Report. In some ways, considering what occurred yesterday, the report just issued is out of date already. But, as always, there is plenty to observe and contemplate.

As far as previous predictions, I was way under in my very wishy washy silver prediction of an increase of several thousand contracts in the total commercial net short position. On the other hand, my revised prediction of a 20,000 contract positioning change in gold was on the mark, particularly as concerned the managed money traders. Truth be told, the gold prediction was much trickier, given large positioning changes within the reporting week. Go figure.

In COMEX gold futures, the total commercial net short position increased by 14,100 contracts to 312,100 contracts, another new bearish record. You'll remember that in the reporting week ended last Tuesday, gold prices had surged to new highs, before reversing. Based upon changes in price, volume and total open interest, in last week's review I had estimated an increase in the commercial short position of as many as 40,000 contracts, as of last Friday.

Due to subsequent price weakness this past Monday and Tuesday, which involved technical fund selling, I trimmed my expected increase to 20,000 contracts. I am convinced both estimates were correct. The commercials sold as many (or more) than 40,000 additional short contracts thru last Friday and then bought back more than half of the new contracts sold on Monday and Tuesday. Since we only have COT reports issued once a week, as of Tuesday, I can't prove to you the intraweek positioning changes are as I represent, but I am convinced that was the case this week. This will go into the update on the running score of the money game that I'll get into later.

By commercial category in gold in the report just issued, the big 4 added nearly 5700 new shorts and the raptors (the smaller commercials away from the big 8) sold another 10,500 contracts short, meaning the big 5 thru 8 bought back 2100 short contracts. The concentrated short position of the big 4 is now at a new record high (182,885 contracts) and despite the buyback of shorts by the big 5 thru 8, the concentrated short position of the 8 largest shorts is also at a new record of 268,041 contracts.

I talk mostly about the concentrated short position in silver (for good reason, I believe), but the fact that only 8 traders hold 86% of the entire record net short position in COMEX gold futures should be setting off alarms and sirens for the regulators. One would think the regulators would have learned the lesson of the past financial crises in which the world was brought to the brink of disaster because too much concentrated risk was held in so few hands (AIG and Lehman Bros.). Should 8 banks be holding close to the entire short position in COMEX gold at this time?

On the buy side of gold, the managed money traders came much closer to my 20,000 contract guess, as these traders bought just over 21,000 contracts, including new longs of 17,436 contracts and the covering of 3732 short contracts. Just as the commercials hold the largest gold net short position in COMEX history, so do the managed money technical funds hold the largest net and gross long position ever. And it is certain that new records have been set through yesterday's trading.

In COMEX silver futures, the commercials increased their total net short position by 8200 contracts to 89,900 contracts. Unlike the case in gold, this is not a new record but closer to the previous high levels seen over the past couple of months. But in no way am I suggesting the level of commercial shorting in COMEX silver is less than obscenely manipulative. By commercial category, the big 4 increased their net short position by nearly 2700 contracts, while the raptors sold out 5200 long contracts and the big 5 thru 8 added the remaining 300 contracts short. Ignominiously, new all-time records were established for the largest concentrated short positions by the big 4 (65,387 contracts) and big 8 (95,612 contracts). Four traders hold 327 million oz of silver net short and 8 traders hold 478 million oz short. Yeah sure ^? these are legitimate hedges (in a pig's eye).

I'd peg JPMorgan as now being short maybe 24,000 contracts, but don't rely on that. The next Bank Participation Report in two weeks should shed more light on this. If there was any ^?good^? news in this report, it may have been that only 3000 new commercial shorts were added, as the majority of the selling was raptor long liquidation. The actual new short selling, moreover, looks particularly small when looking at how many silver contracts the managed money traders bought.

In the buy side in COMEX silver, the managed money technical funds bought a sizeable 14,159 contracts, including 10,589 new longs and the short covering of 3570 contracts. (Non-managed money reporting traders and smaller non-reporting traders accounted for much of the selling this week to the managed money traders). Punctuating the extreme market structure set up in silver is that the managed money traders have never been more long, either on a net or gross basis.

I received quite a few notes accepting my offer to more fully describe the functioning of the managed money technical funds, so I thought I'd answer here. The most frequent question was why these funds would persist in what has been a long term losing game in COMEX gold and silver. A few even questioned if there was not some hidden motive involving these funds losing intentionally. I believe that is far from the truth.

The facts indicate that while my running tally indicates the managed money traders have lost many billions of dollars collectively over the years in COMEX gold and silver, that is not representative of most of these funds' total returns. It is important to remember that these funds are incredibly diversified among many different markets and the assets devoted to and risks assumed in gold and silver make up a very small percentage of total assets under management. In my opinion, losses in gold and silver have been largely offset by gains in other markets ^? that's the whole point of diversification.

In addition, while these funds tend to operate as one, there are a fair number that enter and exit positions at different times, meaning some technical funds can profit individually even while the majority may be losing. For instance, in the big gold price decline in 2013, a number of technical funds got aggressive on the short side early on and scored big returns, even as the majority came out losers. Over the years, those funds whose performance remained subpar did lose assets under management and actually folded or shut down operations.

Still, the managed money technical fund business is a big business. More properly known as Commodity Trading Advisors (CTA's) and registered with the CFTC as such, they managed total financial assets said to exceed \$300 billion. With assets under management (AUM) of that size, even billions of dollars of losses in gold and silver over the years may not stand out, particularly if largely covered by offsetting gains in other markets. As it typically turns out, overall performance tends to be rather subdued and confined to a few percentage points of gains or losses over the years after all is said and done. Here's a snapshot of performance over the years for one of the largest such CTA's, Winton Capital Management. As you can see, performance is usually a few percent per month, positive or negative, with varying annual returns.

<http://ctaperformance.com/wntn>

Managed money technical funds pride themselves as being disciplined and sticking to rigid technical trading principles, which include establishing, holding, adding to and liquidating positions in accordance with the prevailing trend of price. This boils down to buying as prices rise and selling as prices decline. The most important determinant for establishing or liquidating positions seems focused on the relationship of price to various moving averages.

The main thrust of these funds is to lock onto a price trend, up or down, early and then add to that position as the trend persists, finally liquidating when the trend has changed. It is not at all a bad market approach and as I have previously disclosed, some 35 to 40 years ago, I was actively involved as a broker in soliciting and managing client assets in a number of technical funds. I mention this to show I do have some practical hands on experience in this field and in no way do I believe there is any corruption or under-handedness by technical funds in general.

The problem is that these funds have grown too big. It's probably a result of there being massive amounts of investment money looking for returns in a world getting starved for returns; but whatever the reason, the number of these funds and the positions they take have grown too large. "Too large," of course is a subjective term that needs explanation. In this case, too large means the collective positions taken by these funds and their counterparties, the commercials, are distorting prices in many markets, not the least of which are gold and silver. As I have chronicled on these pages, collective technical fund buying and selling of futures contracts has come to be the prime price driver in gold and silver simply because it is the largest buying and selling of all.

Worse, because these managed money technical funds are so rigid in their interpretation of what constitutes a buy or sell signal, it has become fairly easy to anticipate what these funds will do when prices move higher and lower. The ability to anticipate what the technical funds will do has not been lost on their main trading counterparties, the commercials. As I'm sure you know, I believe the price movement in gold and silver has devolved into a sick game where not only do the commercials take the other side of whatever the technical funds buy or sell, the commercials actually orchestrate the technical fund buying and selling through the commercials' ability to rig prices higher and lower through all sorts of computer games.

There is an important distinction to be made here. I don't think the technical funds are corrupt in anything they are doing; it's just their collective positions have grown so large that they have displaced real supply and demand in determining prices. On the other hand, I'm convinced the commercials are corrupt in virtually everything they do, both in gold and silver and just about every business these banks are involved in. The technical funds, at least up until now, have been more dupes and

Date Created
2016/06/25