
March 24, 2018 – Weekly Review

Gold prices surged late in the week and finished close to this year's highs, up \$34 (2.6%), while silver appeared to be dragged along (almost kicking and screaming in protest), ending up 18 cents (1.1%). As a result of gold's outperformance, the silver/gold price ratio widened out to 81.3 to 1. By this relative measure and every other conceivable measure of valuation, silver is stupid cheap and demands to be bought.

The explanation for silver's otherwise inexplicable undervaluation, as well as the absolute levels of and change in gold and silver prices lies in COMEX futures contract positioning, as depicted in the Commitments of Traders (COT) Report. Get ready for a barrage of articles highlighting the current market structures, particularly in silver, featured in yesterday's COT report. Even though the COMEX market structure has always been center stage in my analysis, it's hard for me to believe that with all the things going on in the world today that COMEX positioning is still the central price factor. I'll get into the spectacularly bullish market structure in silver and what likely transpired in positioning since the Tuesday cutoff in a moment.

The turnover or physical movement of metal brought into or removed from the COMEX-approved silver warehouses amounted to just over 4.1 million oz this week, as total COMEX silver inventories rose by 2.1 million oz to 259 million oz, yet another multi-decade high. Most of the total inventory increase was attributed to fresh deposits of 1.7 million oz into the JPMorgan COMEX warehouse, which now holds a record 139.1 million oz.

I know this might sound a little funny coming from me, but I find myself thinking, more and more, that if anything, I may have been understating the amount of physical silver that JPMorgan has and is accumulating. So skilled and determined has JPMorgan been in acquiring physical silver that in COMEX positions alone – including both physical silver in its COMEX warehouse and its new reduced short position in paper contracts – JPMorgan now holds a pretty big net long position in silver. The biggest paper short seller over the past ten years is now net long in pure COMEX dealings and this leaves out the nearly 600 million oz that JPM owns away from the COMEX. How the heck did these crooks pull this off? Yes, that's a rhetorical question.

I haven't mentioned it until now, but there has been a little "stickiness" in this month's deliveries in the smaller silver contract traded on the COMEX, which is based on a single 1000 oz bar. Some 585 mini-contracts have been issued so far this month and all have been stopped by a customer(s) of ADM (the brokerage arm of agricultural giant Archer Daniels Midland) and all the issues have come from the CME Group, which converts the standard 5000 oz contract into 5 mini contracts. A customer of ADM was the sole stopper on 540 mini silver contracts in December.

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

There are 370 mini silver contracts still open in March and it looks like the same customer(s) of ADM is in position to stop those as well. If that occurs, the customer will have stopped 955 contracts (585 plus 370) or 955,000 oz of silver, the equivalent of just under 200 regular contracts. This is certainly not a tremendous amount of silver, but I'm not sure why someone would take delivery of so many mini

contracts, when a smaller number of regular contracts would achieve the same result (I do have some suspicions).

Still, I am intrigued by the budding mini contract delivery drama and my attention to it was magnified when I received some unexpected feedback from the retail front this week. As I'm sure you know, retail demand for silver has been particularly weak for quite some time; so much so that I've stopped reporting on sales of Silver and Gold Eagles. What I heard this week was that a not especially large retail order for a number of 1000 oz bars took some time in securing the bars (getting confirmation of the actual serial numbers). This has occurred in the past and at such times, there were usually other indications of physical tightness.

Combined with the "stickiness" in the delivery process for the mini silver contract, it's hard to come up with an explanation that doesn't point to some tightness in the physical wholesale market. Certainly, in no way does it suggest an abundance of available silver in the form of 1000 oz bars, the form that matters most. Here we have a record short position by technical funds and there are signs of physical tightness in 1000 oz bars. If ever there were signs of a potential silver price explosion, surely they would include a big short position and not enough physical material to go around.

The changes in this week's COT report were almost exactly as expected in gold and almost exactly what I hoped for in silver. As a reminder, price action during the reporting week ended Tuesday was as close to perfect salami slicing as any I've seen, in that slight new price lows were achieved every single day in both gold and silver. To a managed money technical fund, this is a motivation to sell that is irresistible.

In COMEX gold futures, the commercials reduced their total net short position by 21,500 contracts to 167,300 contracts (I had predicted 20,000 contracts on Wednesday). This was the lowest (least bearish) total commercial headline number since late December. All the commercial categories bought, but it was mostly a raptor (the smaller commercials away from the 8 largest shorts) affair. The big 4 bought back only 800 short contracts and the big 5 thru 8 bought back 2900 short contracts, while the raptors added 17,800 new longs to a net long position amounting to 61,800 contracts as of Tuesday.

On the sell side of gold, it was an exclusive managed money affair, as these traders sold just over 24,000 net contracts, including the sale and liquidation of 14,185 long contracts as well as the new short sale of 9,873 contracts. While this managed money selling was as expected and set the stage for the sharp rally that commenced on Wednesday, yesterday's report was, well, yesterday's news, in that there has likely been massive managed money buying since Tuesday. How much buying? I'd say 40,000 net contracts or more through Friday's close. That would still leave gold with a neutral to bearish market structure.

In COMEX silver futures, the commercials reduced their net short position by a massive 15,600 contracts to 3,700 contracts (I had guessed a 5,000 to 10,000 contract reduction and hopefully more, so the change was twice my blended guess - he said as he tried to hide his glee). In essence, this is the lowest (most bullish) commercial headline number in history and incorporated in the report were any number of other historic extremes.

By commercial category, the big 4 bought back 4,000 short contracts, while the raptors added 13,500 new long contracts to a net long position now amounting to 73,200 contracts, another new record. The big 5 thru 8 added 1900 new short contracts, but the selling was done by managed money traders and

not commercials. I'd peg JPMorgan's short position to be down to 21,000 contracts and, likely, even lower than that. This is the lowest paper COMEX short position held by JPM since last summer and combined with their 700 million oz physical silver holdings leaves JPMorgan net long by 600 million oz, the most ever.

On the sell side of silver, as was the case in gold, it was strictly a managed money affair as these traders sold an astounding 19,418 net contracts or nearly double the higher end of the range I was expecting; comprised of the sale and liquidation of 5,666 long contracts and the new short sale of 13,752 contracts. On a one week decline of around 45 cents in the price of silver, the managed money traders sold the equivalent of nearly 100 million oz of metal. That should bother everyone, not the least of which being the regulators since, by their own definition, this was all speculative selling with not the hint of legitimate hedging.

Historical records were shattered all around, including the largest gross managed money short position ever, at 68,432 contracts, as well as the largest net short position at 35,833 contracts. Not an all-time record but close to the lowest levels in years, the managed money gross long position of 32,599 contracts, now 4000 contracts below what I considered to be the core non-technical fund managed money long position set recently. Again, I wouldn't mind the managed money long position going as low as there are numbers because once sold, the bearish impact on price is gone forever. It's just hard for me to conceive of what, at this time, could have persuaded the managed money traders to hold their lowest long position in years.

But it was the managed money short position that nearly took my breath away; so much so, that I can't help but wonder how it came to be. In other words, I can't help but question what possessed these traders to go as heavily short as the new report indicates at this time and place and price in silver. Don't misunderstand me, I am absolutely ecstatic that such a large load of built-in buying power that can only be described as rocket fuel has been created in silver; I'm just wondering how the heck the commercials pulled this off and the managed money traders fell for it hook, line and sinker.

I believe I know as well as anyone how this COMEX positioning scam works, but I am still in near shock at just how much potential danger the managed money shorts have placed themselves. It really doesn't matter how the managed money traders came to be as heavily short in silver as the new COT report indicates, no one should doubt the report's veracity. While I wouldn't doubt some extra-special and behind the scenes influence by the commercials to encourage the managed money traders to plow onto the short side in silver this time, I believe there is something more basic in play.

I think mostly it has to do with the managed money traders becoming too comfortable with their own trading experiences in silver. While they are now holding a record net and gross short position in COMEX silver, this is not the only time these traders have been heavily short silver over the past few years. Basically speaking, while the managed money technical funds have never collectively profited when operating on the short side of COMEX silver, neither have they ever suffered catastrophic losses in being heavily short.

We're all captive to learning from our own experiences and the technical fund experience in COMEX silver has taught them that no great harm will befall them in shorting silver, even if they haven't been graced with big profits either. So many times have the managed money traders sold silver short below the moving averages and then closed out those short sales slightly above the

moving averages that I believe they have no conception of the real risk that lurks in shorting silver. Therein lies the rub.

Individually, I suppose, a managed money trader's risk in shorting silver is one issue; but I'm talking about something entirely different, namely, the fact that enough managed money traders have shorted silver that it has created a collective risk. The picture in my mind to describe this is of the managed money traders positioning themselves on the limb of a large tree and then proceeding to saw off the limb and expecting the tree to fall, but not the limb they have just severed. The managed money traders seem oblivious to the collective risk their massive short position places them in.

Only the constant repetition of being similarly positioned in the past and having always been able to escape with no financial disaster can explain the managed money traders willingness to stick their collective heads back into the lion's mouth. I know these funds completely eschew any thought of actual supply/demand fundamentals or value associated in the commodities in which they trade and rely on price change alone and that's a big part of the potential problem they face.

Not only are the managed money traders avoiding questions of over or undervaluation in their trading, they show no hint of recognizing that the extreme size of their collective positions in relation to the size and nature of the fish pond in which they operate. One never wants to be the biggest fish in a small pond unless one is in complete control (like JPM).

Remarkably, just as interest in COT market structure analysis has achieved record attention, it doesn't seem possible that any managed money trader has a clue to what's contained in the COT reports. This despite the fact that the managed money traders are the key trading force and must report every trade they make. It's as if everyone is watching the managed money traders for extremely reliable clues about the markets except the managed money traders themselves. This is what creates the potential for financial disaster for these traders.

Certainly, the managed money traders seem particularly oblivious of who is on the other side of their positions, namely, the commercials who live off them like leeches. Otherwise they never would have allowed their collective positions to grow so large. Craziest of all is that the managed money traders maintain their trading accounts at the same large commercials which are bleeding them dry, in particular, JPMorgan, which gives the commercials a further leg up and puts the managed money traders at further disadvantage. JPMorgan knows exactly how the managed money traders operate and are likely to behave; the relationship is not mutual.

The combination of the massive size of the collective managed money short position in silver plus their complete dependence on counterparties who stand to benefit the most should the greatest financial loss befall the managed money traders sets up the possibility (likelihood) of a discontinuous event - a bolt out of the blue in the form of a silver price explosion. All the necessary ingredients are in place. One of these days, Alice, it's pow to the moon. In simple terms, this is why I throw good money away on out of the money call options - I know the explosion is coming, even if I can't say exactly when.

As I indicated above, in trading action since the Tuesday cutoff, I would estimate that at least 40,000 net gold contracts have likely been purchased by the managed money traders as prices surged above the one key moving average (the 50 day) that had been recently penetrated to the downside. This puts the market structure in gold to being on the bearish side, but still more than capable of further gains

amid continued managed money buying. It doesn't look likely that the 200 day moving average in gold will be penetrated to the downside after the rally of the past three days, but if the commercials decide such a price smash is required, it will come. After all, when it comes to gold and silver prices, the commercials have been in charge.

While there is strong evidence pointing to heavy managed money buying in gold over the past three trading days, no such evidence exists in silver. In fact, the flip side to the relatively rotten price performance in silver relative to gold, is that it strongly suggests no net managed money buying has occurred in silver. Based upon previous managed money behavior, any time silver trades consistently below its key moving averages and then rallies up to, but not penetrating those moving averages to the upside, there is a good chance of additional managed money selling on that rally.

The reason for this is as discussed above, namely, new short sales closer to the moving averages (but not above those averages) are perceived by the managed money traders to be less risky because the buyback close out point is much closer, meaning that the perceived risk is smaller. Admittedly, this approach has mostly worked for the managed money traders over the years, in that these traders have always been able to avoid financial disaster when being heavily short silver in the past. But one day, I'm convinced, this approach will prove even more catastrophic than the managed money traders can begin to imagine.

If there's any logic behind expecting the silver price explosion to occur when it is most disadvantageous to the managed money traders and most advantageous to the commercials, particularly you know who, the time has never been riper than now, according to the data in the COT report. Accordingly, I have spent the last of my mad option money created out of sidestepping the price decline into December. I'm good for a couple of months, but if silver hasn't exploded by then, I'll have to dig down and round up fresh funds. On a non-option basis, I am and have been as all-in as it gets.

Ted Butler

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Silver – \$16.58 (200 day ma – \$16.78, 50 day ma – \$16.70)

Gold – \$1348 (200 day ma – \$1292, 50 day ma – \$1331)

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