

March 8, 2017 – Still the One

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A funny thing happened on the way to the end of the COMEX's price domination for all things gold and silver – that price dominance got a lot stronger. So much so that it's hard to detect the presence of any other price influence, including China, India, Russia, London, actual supply/demand, the Fed, the new president or the man in the moon. I still believe the COMEX's long term price control will lead to shockingly higher prices, particularly for silver, but I am thunderstruck when observing just how much stronger the control of the COMEX has grown with each passing day.

There is no shortage of evidence that what happens in COMEX futures contract positioning has become the prime, if not sole driver of price. It can be seen in the almost universal attention paid to the current near-record bearish market structure in COMEX silver, where the last COT report indicated massive managed money long and commercial short positions. Never have I seen more specific references to this highly-specialized fact of market life. Most remarkable of all is that the attention to the COMEX market structure is well-deserved and justified.

For my part, I still think it comes down to two main COMEX – either or's – how the massive managed money silver long position gets resolved and how the rest of the COMEX March silver deliver period plays out. One is a paper trading question, while the other is largely a physical market resolution. Let me deal with the March COMEX silver deliveries first.

Here's what the data show after the first 7 days of delivery; there have been 1905 total silver contracts delivered (including redeliveries which tend to overstate the total by a bit). That's a little over 9.5 million oz. Of the total silver deliveries issued so far, JPMorgan has taken 1197 contracts in its own name and another 420 contracts on behalf of a client(s). Combined, JPM and its client(s) have taken physical delivery on 1617 silver contracts, or 85% of the total issued to date.

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

By and large, JPMorgan has been the largest stopper or taker of COMEX silver deliveries for the past 3 years, mostly in its own name but also at times in combination with clients. Much of these deliveries were then transferred into JPM's own COMEX warehouse and explains why the total amount of silver there is more than 90 million oz, making it the largest warehouse in the COMEX system, and accounting for nearly 50% of total COMEX silver inventories (it started at zero ounces in 2011).

According to my analysis, the 90 million+ ounces in the JPM COMEX warehouse constitute about 15% of the 550 million ounces I claim the bank has acquired over the past six years. Some may disagree with that, but no one could argue with any of the JPM/COMEX data that I just presented. As I have mentioned in the past, the key question I have in advance of every traditional COMEX silver delivery month (five per year) is what will JPMorgan do — stop, issue or stand aside on that month's deliveries. Since JPMorgan has been the big COMEX silver delivery stopper for years, I can't say I was surprised that it has been the big stopper this month as well.

But it isn't the number of silver contracts or the percentage of total deliveries that JPMorgan has thus far stopped in the March deliveries that causes me to highlight this particular delivery month as the tightest I've seen in my decades of observing this data closely. Instead, it is the number of contracts remaining open in the March futures contract that stands out. As of the close of business yesterday, some 2000 contracts remain open, a number unusually high at this point in the delivery process. Moreover, based upon the number of deliveries assigned to JPM and its client(s) over the past few days, it would appear that JPMorgan and its clients own nearly all of the remaining 2000 open contracts in March.

First, let me tell you what I'm not saying — I'm not saying there will be a delivery failure or contract default in March silver futures. That is almost unthinkable, not the least because it would be inconceivable to imagine JPMorgan, the leading clearing firm on the COMEX, as ever allowing such a default. After all, JPMorgan would have the most to lose in such a delivery default (apart from the tens of billions of dollars it would make on the silver price explosion that followed a delivery default). After all, JPMorgan has been in this precise delivery circumstance once or twice before and always — backed down — and relieved any delivery congestion by voluntarily liquidating any remaining open contracts that might force shorts to fail to deliver or accommodating the shorts in other ways (such as agreeing to an EFP — an exchange for physical delivery transaction).

So if I'm not suggesting there will be a delivery default in March COMEX silver because the short sellers might not be able to physically deliver the metal that JPMorgan or its clients have already contracted to receive, then what am I saying? I'm saying that I'm amazed that it has been taken this far already this month. COMEX silver (or gold) deliveries are among the most, if not the most transparent methods of acquiring (or disposing) of metal. This is particularly true when a COMEX clearing firm takes or makes delivery in its own name, as that additional information has to be disclosed. Most amazing of all is that JPMorgan has turned into the most transparent acquirer of physical silver on the COMEX, only after I identified the bank as accumulating massive amounts of Silver Eagles and metal from the SLV.

Even if JPMorgan backs down completely from this point and lets the shorts in the March futures contract off the hook from having to make physical delivery on all the remaining open contracts, that won't erase what has been learned to this point. In addition to the large number of contracts remaining open and JPM's likely concentrated ownership of those contracts, there have been signs of stress on the part of the shorts which have already made delivery. It seems most of the silver delivered this month has come from metal brought into the COMEX warehouses over the past week or so or recently transferred from eligible status to registered status. This suggests the shorts didn't deliver metal just laying around or with metal earmarked and intended for delivery at the time of the original short sale; but rather with metal that had to be secured at the last minute, perhaps due to unexpected delivery demands from JPMorgan.

No matter how the March COMEX silver deliveries are resolved by the end of the month, enough has been learned to this point to conclude this is a very tight delivery period. This is not the kind of data that I would expect most observers to focus on, but to anyone paying close attention, the conclusion points to physical tightness in silver. Yet to this point, it seems overlooked even on the part of those entities in direct competition with JPMorgan, such as other COMEX clearing firms. If it were otherwise, JPMorgan wouldn't be the near-sole stopper of COMEX silver deliveries this month or all the previous traditional delivery months over the past 3 years.

For the life of me, I can't figure out why JPMorgan has allowed itself to have been so completely open about its accumulation of physical silver by way of COMEX futures deliveries. I can understand folks not zeroing in on the bank's clandestine accumulation of metal via Silver Eagles or share to metal conversions from SLV, but taking delivery on the COMEX is the most transparent process of all. That JPMorgan would be so open on this most transparent of delivery methods is mind boggling. Forget the 450 million+ ounces of silver JPM has acquired from other sources; the 90 million+ oz accumulated on the COMEX is enough for me (or anyone) to call this bank a super crook. What else would you call the dominant physical silver stopper while it is simultaneously the largest paper short seller?

In summary, while I don't expect a delivery default in COMEX silver this month, I am genuinely surprised at the clarity of the data and the unmistakable message it sends about physical tightness. I would expect JPMorgan to quietly arrange to let the shorts off the hook in some way (perhaps Exchange for Physical transactions) but that won't erase the telltale signs of physical tightness already revealed. Still, the March delivery process is still an either or – either JPMorgan accommodates the shorts or it doesn't.

The other big separate COMEX issue is whether the newly-added managed money silver long positions get fully flushed out or not. To be sure, the price action this week suggests the technical funds are being flushed out, as not only have the commercials been able to rig prices lower through the 200 day moving average in silver starting last Thursday, prices are now dancing on the 50 day moving average in both silver and gold. In addition to fairly high trading volume on the decline, the very familiar pattern of consistent new lows (salami-slicing) has been undeniable.

As such, it is reasonable to assume there has been a fair amount of managed money selling in silver and gold. The correct question is how much and, more to the point, how much additional managed money selling remains. In gold, the high volume and pronounced salami slicing to the downside has come from a market structure not at all that bearish to start with. It has only been during the last two COT reporting weeks that the managed money traders bought and the commercials sold notably in gold, particularly in last week's report.

These new gold longs are underwater and it's reasonable to assume many or most of the new gold longs have already been flushed out. We may not see that completely in Friday's COT report, as the selling has continued past yesterday's cutoff for the report; but my point is that there weren't that many managed money gold longs to be flushed out to begin with and, therefore, there can't be that many left to sell.

The story is different in silver, where we went into the selloff that began a week ago with near-historic managed money longs on the books. This translates into potential managed money selling in silver much greater than existed in gold. Since this whole concept of market structure analysis has taken hold to a degree hard to fathom, I suppose it's not surprising that I have read more recent commentaries than ever before pointing to the conclusion that silver will selloff hard as the managed money traders rushed to sell.

Surely, the silver and gold selloff over the past week and any further selloff is and will be due to the managed money traders selling into the price prompts given them by the banks and therein lies the reason why we have gone lower and may go lower still. A complete managed money flush out would likely entail another dollar or so in silver and a somewhat less relative potential decline in gold. This was always one of two potential outcomes.

The other alternative was much less than a complete managed money flush out in silver, with a significant number of newly added technical fund longs refusing to sell off on bank price rigging to the downside. According to my alternative premise, a good number of managed money traders may have awoken to the fact that they had been played by the banks for decades. Under the worm had turned premise, we still might see sharp price takedowns, but later evidence would indicate only some of the newly-added longs would be sold and when that was recognized by the 7 big commercial shorts, those shorts would panic instead.

As far as I can tell, the evidence of complete managed money selling in silver is yet to be determined. It's not the same in gold because there was no similar build up in managed money longs as there was in silver. To my mind, the commercials have taken gold lower simply to aid in liquidating the maximum number of managed money longs in silver. Considering how much larger the gold market is compared to silver, I suppose it may sound extraordinary to suggest the banks have rigged gold lower to aid in pressing silver lower. That is, until you try to construct an alternative explanation for why gold has been so weak. And it's not extraordinary at all when one peers into the real circumstances in silver.

One good thing about this sharp selloff (in terms of ripping a band aid off quickly or slowly) is that it should bring closure to my either or premise. We'll soon see the evidence of whether we'll have a complete or only a partial liquidation of the newly added managed money silver longs. I would have preferred that silver would have moved immediately higher, but a second preference would be to resolve the matter quickly, rather than have it play out for months. This week's price smash should at least grant the second preference.

A complete managed money flush out in silver will, at least, bring us back to a point where there will be little remaining risk and where the prospects for the next move being the big one are flashing. That will involve more price pain and the acknowledgement that the technical funds haven't wised up as I've suggested. It will also preserve my record of being premature about the big move higher, but nonetheless will offer another outstanding opportunity to buy silver.

If instead, we are currently witnessing a near completion of a partial liquidation of the newly-added managed money silver longs, then my crazy premise may still be alive. If say, only 15,000 contracts of the 40,000 total contracts of managed money long positions in silver added since late December that were going to be liquidated are, in fact, already liquidated (possible) — then there is little reason for silver prices not to quickly turn higher. And we would only get to this point in a sharp price takedown as occurred this week.

One thing that shouldn't be underappreciated is the growing attention to COMEX market structure issues. I'm seeing those who never raised the issue before offer convincing arguments on what it means to prices. It's rare when you see many talk about the right issues in anything. And while it's not completely acknowledged just yet, I feel it is only a matter of time before those discovering the importance of COMEX futures positioning will also recognize just how crazy it is to have speculative positioning as the sole determinant for price. Perhaps more than anything else, it is this growing recognition about how silver and gold prices are set that promises to undermine the artificial COMEX price-setting. On the other hand, it is folly to claim, based upon the evidence, that COMEX price-setting has never been stronger.

As far as Friday's COT report, without putting actual numbers on it, I will be surprised if we don't see the biggest reductions in managed money long and commercial short positions in months. Additionally, Friday's Bank Participation Report should help clarify JPM's silver short position. While I'm sorry I didn't sidestep this blatantly engineered selloff, the truth is I would have also reentered just as quickly given the signs emanating from the March silver delivery month and my still open premise about a partial managed money liquidation. At least there should be no question about why we've moved lower.

Ted Butler

March 8, 2017

Silver – \$17.27 (200 day ma – \$18.01, 50 day ma – \$17.28)

Gold – \$1209 (200 day ma – \$1263, 50 day ma – \$1208)

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