March 9, 2016 – Still Only One Negative

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My goal is to explain the silver and gold markets, based on the most important and reliable data available, to best prepare for future price levels. Over time, my explanation has become, by necessity, repetitive, yet specific. After all, if one studies an issue for a long time, he or she shouldn't develop new basic and very different premises to explain a particular phenomenon on a regular basis. It's fine to incorporate new developments into a general premise, but not to the point of re-inventing the basic theory of the case at every turn.

My basic premise is that the actual supply/demand fundamentals of silver guarantee much higher prices and the only reason the price is not already at those much higher prices is because of an ongoing price manipulation on the COMEX. This same COMEX price manipulation also strongly affects the price of gold, but there are important differences between the two metals, which convince me that not only will silver soar in price, it will soar in price relative to gold. Even though, admittedly, that has not been the case of late.

The main difference is that silver is a versatile and vital industrial commodity and its use as such not only restricts the new amount of metal available for investment on a current basis, but past industrial consumption has resulted in the seemingly preposterous circumstance that there is now less recoverable silver above ground in the world than there is gold. I say Â?preposterousÂ? circumstance because who ever imagined it possible in comparing two similar items that the item which is rarer costing less? And not only does silver's industrial demand explain why it is rarer than gold, the accepted world inventory data on each also confirm the preposterous circumstance that there is, effectively, less silver in the world than gold.

Recently, I commented that we are close to the most undervalued silver has been relative to gold, not just in a long time, but in recorded history. Were silver to trade at more than 100 times per ounce compared to gold (from its current 82+ ratio), as it did in both in 1991 and in the 1930's, it would set an undervaluation extreme never seen in 5000 years. That's a long time. Since silver, in practical physical inventory terms, is rarer today, relative to gold, than it has ever been in history, the current price ratio would seem to be inexplicable; or at least require an explanation worthy of the extreme relative price conundrum.

There is such an explanation and it revolves around the COMEX futures contract positioning between the commercials and the managed money technical traders and as detailed in the Commitments of Traders (COT) Report. It is this positioning which exerts the greatest influence on silver and gold prices in the here and now and not actual metal supply/demand developments. So great is the COMEX market structure influence on price that I am both amazed, but not really surprised, by the growing awareness and commentary about the COT data.

Where, say only a few years ago, most Internet commentary skipped over COT considerations, that has clearly done an about face and today such commentary seems to be the primary focus. I would hold this is how it should be, considering the history and rationale behind the data. Previously, I commented that I have come to dismiss analysis that ignores COT data because the data are so important. Now, because there is such an increase in COT commentary, we may have come full circle. Recently I read commentary that complained that too many COT Â?expertsÂ? were cropping up, when the commentator himself was relatively new to the fold.

That said, until proven otherwise, the COMEX market structure as defined by the COT report should be relied upon as the most powerful short term price force. There is no doubt in my mind that this price force is purely manipulative, but I'll save this angle for another day. As I hope I have been conveying, the COMEX market structure has become extremely bearish in both gold and silver and when similar bearish structures have occurred in the past, the probabilities favored lower prices.

What makes the current bearish readings more unusual is that the COT readings are the only bearish factor in place, particularly in silver, but also in gold. I suppose this is almost always the case, but I am referring specifically to the extreme disparity between the bearish COT readings and the newer developments in silver I have highlighted recently. Since the only bearish factor is the current COMEX market structure, let me first discuss the newer bullish developments in silver and how everything may be related.

One the newer factors in silver is the ongoing COMEX March silver delivery process. We are into the second week of the delivery process and the data to date indicate the unmistakable footprints of JPMorgan's typical dominance of all things silver. It's clear now, from continuing daily CME data, that JPM came into the delivery month in position to stop or demand the maximum number of silver contracts allowed Â? 1500 contracts (7.5 million oz) – for both itself and on behalf of a client; a total of 3000 contracts or 15 million oz. This coincides with my basic premise of JPMorgan accumulating massive amounts of actual metal over the past 5 years, now amounting to more than 400 million oz.

Apparently, JPMorgan ran into a snag in its plans to acquire 15 million additional ounces of metal in the March delivery period as it has subsequently and voluntarily liquidated many of its open March contracts. At this point, it looks like JPMorgan has liquidated more of its customer's remaining March long positions than its own positions, but I can't imagine anyone being surprised by that. The most plausible explanation for the snag or change in plans in JPM taking delivery on as many as 3000 combined contracts is that the sellers weren't in position to make delivery. The short holders of the March contracts weren't able to meet JPMorgan's demand for physical silver without disrupting the price (to the upside); and, rather than risk the overall stink of a prospective short squeeze, JPMorgan backed down on its delivery demands.

We went into the first delivery day with more than 3400 March contracts open and, I can claim now, that JPM held 3000 total longs in March (despite being overall big net short in COMEX futures contracts). But after 8 delivery days, only 339 contracts have been delivered so far, a shockingly low number for what is a traditional COMEX silver delivery month. By comparison, there have been 576 deliveries this month in COMEX gold and March is definitely not a traditional gold delivery month. What's the most obvious reason for the lack of deliveries in March silver? The shorts didn't have or can't secure the physical material easily.

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

Of the 339 March deliveries issued so far, JPM and its client(s) have taken (stopped) 286 contracts or 84% of the total issued. The remaining open interest in the March futures contract is down to roughly 1500 contracts, meaning since the start of the month as many as 1500 contracts were voluntarily liquidated or rolled over by JPM. Based upon a noticeable tightening in the spread differentials involving the March contract, the short holders in that contract have been more aggressive in buying back their shorts than has JPMorgan and its client in selling their longs.

In essence, it appears that JPMorgan is letting the March contract short holders off the hook as far as making physical delivery of silver. Why would JPM do that? After all, if I am correct, JPMorgan owns more than 400 million oz of physical silver and as such would stand to gain mightily on a rise in the price of silver, even if it is still short 90 million paper oz (18,000 contracts) on the COMEX. JPMorgan has never been better positioned for a liftoff in the price of silver than it is now; yet it has just taken action (in letting the March silver shorts off the hook) that has prevented a short squeeze from developing on the COMEX. Again, why would JPM do this?

The only explanation I can come up with is one in which JPMorgan benefits from its own actions. This has nothing to do with anything other than what's good for JPM. Simply put, JPMorgan stands to benefit more by letting the March COMEX shorts off the hook and by not causing silver prices to soar at this moment, even though it would make more than anyone should prices soar. The one thing that would convince JPMorgan to forego picking up a decent additional chunk of physical silver that it already contracted for would the prospect of buying even greater quantities of silver at even cheaper prices. How can it benefit JPM to let loose of the silver bird in its hand in order to pick up more in the bush? Please let me explain.

By letting the March silver shorts off the hook and averting a delivery squeeze that surely would have lit a fire under the price of silver, JPM has set the stage to buy much more silver in paper form in COMEX futures. Remember, despite the very pleasant surprise that JPM hadn't increased its net COMEX silver futures position as of Tuesday a week ago, it was still net short, by my calculations, 18,000 contracts or the equivalent of 90 million oz.

Buying as many of those short contracts back on lower prices as possible would be of the most benefit to JPM at this time. If JPMorgan can buy back, for instance, 8,000 to 10,000 of its short COMEX contracts, that would have the same financial impact to the bank as buying an additional 40 or 50 million oz of physical silver. Yes, I know there is a difference between paper silver and real silver, but not to JPM in this case.

There is no way that JPMorgan could buy 40 to 50 million oz of physical silver in a hurry without launching the price skyward, considering that it just backed down on demanding much less of a quantity in the March deliveries over concern of what that would do to silver prices. But in a deliberate price rigging to the downside, which would likely set off an orgy of managed money technical fund selling, JPMorgan has (on many past occasions) and most likely could buy back a significant percentage of its remaining paper short position.

If JPMorgan succeeds in arrange such a price selloff, the potential benefit to the bank would be immense. It would also be about the most bullish thing that could occur in silver, to my mind, since it would appear to remove the last obstacle for a silver price liftoff. Along with JPMorgan not adding to its silver shorts through last Tuesday, for the first time ever, a significant reduction in the bank's existing short position would be bullish beyond description.

Unfortunately, you can't make an omelet without cracking some eggs and neither can JPM nor the other commercials buy silver (and gold) contracts without technical fund selling. And since technical fund selling only occurs on lower prices, it would appear that lower prices would be the commercials' plan. There is no guarantee that JPM and the commercials will succeed in arranging a selloff, but history appears to have been on that side. This brings us to the only bearish factor that I can see Â? the current market structure according to the COT report.

Based upon the current market structure, I've seen predictions for a certain selloff and other predictions that the commercials will fail this time and get overrun. Both sets of predictions are made with equal implied certainty and seem made to achieve maximum benefit to those making the correct prediction. I'm not smart enough to predict with guaranteed precision, but I'm comfortable with the idea that things will likely work out in a way that most benefits JPMorgan. That's what I mean when I say the probabilities favor lower prices on COT considerations alone.

As far as what the new COT report will indicate when it is released on Friday, I can't see how there won't be a massive increase in commercial selling and managed money buying, particularly in COMEX gold futures. Gold prices surged as much as $50 to new one-year highs on heavy volume through the reporting week ended yesterday. Total gold open interest data, surged as well, up nearly 50,000 contracts through yesterday's cutoff. This implies a large increase in the total commercial net short position, perhaps by an amount approaching the increase in total open interest, but probably not less than 30,000 contracts.

Silver's total open interest increased by more than 7000 contracts, amid a price surge and volume increase (particularly on Friday) and, accordingly, I would anticipate an increase in commercial selling approaching the increase in total open interest. If we do see such big increases in commercial selling and managed money technical fund buying, that would put the gold and silver market structures at even more extreme bearish readings. That strengthens the probabilities of a price decline.

A long term subscriber wrote to me this week, encourage by the news that JPMorgan hadn't added to its silver short position for the first time ever on a price rally, but was concerned by the still large total commercial short position in silver. He has, in my opinion, good reason to be both concerned and encouraged.

If we do get an eventual price resolution to the downside, as the COT probabilities suggest, the actions of JPMorgan (described above) do suggest, more strongly than ever before, that this will be the final selloff. That is, if JPMorgan succeeds in buying back and closing out a significant portion of its COMEX silver short position, it would then appear to be ideally positioned for silver price fireworks to the upside. I suppose the fireworks could come sooner and that JPMorgan won't be able to buy back a big chunk of its silver shorts on lower prices, but then again, the world of silver seems to resolve around what's best for JPMorgan.

Ted Butler

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Silver – $15.30 (50 day moving average – $14.63)

Gold – $1253 (50 day moving average – $1155)

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