
May 16, 2018 – Into Sure Thing Territory

Yesterday's waterfall decline in precious metals prices pushed gold to a loss for the year and below both its key 200 day moving average as well as the very round number (\$1300) it had held above for all of 2018. Silver prices also fell proportionately, but have been trading mostly below the same moving average for much of the year and so far have yet to penetrate the \$16 price handle. I suppose if one was inclined to view things in conventional technical chart terms, the breakdown in gold would be considered somewhat ominous and portending further substantial price declines ahead.

But if one viewed gold and silver prices as being driven by COMEX futures contract positioning, as I do, yesterday's high volume trading action was nothing but good news if you are bullish inclined. In fact, it was just what the doctor ordered for a precious metals bull like myself. Don't misunderstand me, I'm sensitive to the erosion in the value of silver investments of those fully invested (like myself), as it's never fun to lose money, even temporarily. And I'm more than annoyed that prices are so openly manipulated by speculative paper trading in full view of the do-nothing regulators at the CFTC. But analysis is about projecting where prices are likely to be, not where they have been (much like how the Great Gretzky considered the hockey puck). In terms of COMEX positioning, yesterday (and today) was nothing but good news for those expecting higher gold and silver prices.

Yesterday's trading activity was significant enough so as to push gold and silver into sure thing territory in terms of higher prospective prices. Admittedly, those are very strong terms, so let me be explicit in what I'm suggesting. Certainly, I can't guarantee prices won't slip slightly lower in the very short term as COMEX positioning is a process, not an exact predictive calculation. And if prices do slide a bit lower, then that only makes the market structure that much more bullish. The most important variable in the sure thing equation is how many more contracts can the brain dead managed money traders be hoodwinked into selling by the commercials. While I will get to that variable component of the sure thing equation in a moment, let me first deal with the constant component of the equation; the component on which the sure thing rests.

Yesterday's waterfall price decline was not caused by selling by the cartel or any combination of central banks and/or bullion banks seeking to suppress the price of gold and silver and it is downright painful to continue to read such stories on the Internet at this late stage. This game is all about the money changing hands on the COMEX and, accordingly, must be evaluated by following that money. The selling was done exclusively by the managed money trading category, as will be shown in this Friday's Commitments of Traders (COT) report.

Yes, it is quite true that the commercials induced the managed money traders into selling aggressively yesterday by rigging prices lower through a variety of dirty trading tricks (including some early light selling to get the snowball rolling downhill); but it must be remembered that the commercials (and other traders) were the big buyers yesterday, same as on every big price decline practically since the dinosaurs roamed the earth. Never, never, never have the commercials ever been net sellers on a big price decline in gold and silver (based upon historical COT data).

Armed with the certain knowledge that the managed money technical funds were the big sellers yesterday, we also know that these traders have been on a selling spree recently in gold and silver as also is evidenced in COT data, making yesterday's price plunge the perfect salami slice invitation to sell that no managed money technical fund could resist. Going into yesterday, the technical funds had already been notable sellers, with the managed money traders holding their lowest net long position in gold since July and close to their largest net short position in silver in history.

Therefore, I would not be surprised if this Friday's COT report indicates that the managed money net long position in gold is at its lowest level since December 2015. Back then gold was trading around the \$1050 level and about to embark on a \$300 rally into the summer of 2016 as the managed money traders bought nearly 300,000 net contracts on that rally. There is nothing to suggest that when the next gold rally gets rolling that the rally won't be even more pronounced. Let me stop here to make a point about gold, even though I am a diehard silver bull who holds only silver.

While I am adamant that COMEX positioning is the prime, if not sole price driver of gold and silver prices on a here and now basis; over longer periods of time other factors influence price, like investment flows into actual metal. I would like to point out something that shows that in gold. I just stated that the new COT report will indicate that the managed money net long position in gold is likely to be the lowest it has been since December 2015 when gold was priced at \$1050. In hindsight, that proved to be the market structure set up that accounted for a \$300 rally over the next six months.

Now, here we are at close to the same low level of gold managed money longs (actually there was a small managed money net short position back then), only the price of gold is closer to \$1300 or \$250 higher than it was back in Dec 2015. What accounts for the much higher gold price when the COMEX market structure is positioned very close to what it was back then? I would say physical investment flows and actual supply/demand considerations. Almost unseen on a day to day basis, the demand for physical gold has caused the price to be hundreds of dollars higher over the past couple of years, undoubtedly connected to the physical demand coming from the East. Now if you ask me why that isn't evident in silver, my answer would be because silver is much more manipulated than gold has ever been; but when the day of reckoning comes in silver, you'd best stand back if you're not aboard.

Back to the sure thing equation. What makes me look at gold and silver in the sure thing category for a much bigger rally than any price decline from here is the nature of the managed money/ commercial contest. Simply put, the commercials always win and the managed money traders always lose, at least in COMEX gold and silver. Recently, I highlighted how JPMorgan, alone, had made about \$400 million in COMEX silver futures trading over the past year. But when you include the other commercials (mostly the smaller raptors) and trading in gold, the amounts made by the commercials collectively (now also including the other large non-reporting traders) are many times the amount made by JPM in silver. Every penny made by the commercials, basically, comes from amounts lost by the managed money traders, because futures trading is a zero sum game - whatever is gained must come from someone who has lost.

So one key feature of the sure thing equation is that the traders which have always lost in the end, the managed money traders, are now heavily configured on the short side, indicating if they continue to do what they have always done in the past, namely, lose, it will be because gold and silver prices rise, causing these traders to buy back the contracts they have sold at higher prices than sold at originally.

On higher prices, those then selling to the managed money traders, the commercials, will again make a profit.

Most typically, the managed money traders hold net long positions, often quite large, while the commercials have always been net short in gold and silver, also often in quite large quantities. Now the managed money trades are still net long in gold (not in silver), but to a very low level, while they are much more short than typically and even more so when Friday's report is published. Although the managed money traders have always lost in the end when they have been heavily long gold and silver, they have often held those big long positions at very large open or unrealized profits, only to give up all those open profits eventually.

You may remember how I reported on the big open profits of the managed money traders long silver and gold and the corresponding open losses held by the commercial shorts throughout the summer of 2016. The managed money traders were ahead by some \$4 billion into the summer, meaning the commercials were out by that same amount. But by the fall and winter of 2016, the managed money traders lost all their open profits and the commercials recouped all their open losses as gold and silver prices fell precipitously by yearend.

But the managed money traders, when heavily long in gold and silver, at least had a chance of breaking the never-ending cycle of losing in the end, as I also reported at the time and over the years. At such times, the possibility existed of a commercial overrun to the upside, due to a black swan-type event. Although it has never happened in gold or silver, there are examples in other commodities where the managed money traders continued to do well after establishing a big long position. One such example is occurring in crude oil, where after the managed money traders established a big long position and stopped buying, other factors have caused the price of oil to continue to rise. But that has never occurred in gold or silver, to my knowledge.

If the managed money technical funds had some chance of lucking out after establishing big long positions in gold and silver, I see no such chance of that occurring when they are very light on the long side and very heavy on the short side, like now. These traders stand almost no chance of ever demanding actual delivery when they are heavily long and much less chance when heavily short. Therefore, the managed money traders short gold and silver have only one way to undo their short positions and that is by buying back those short positions. The only question is at what price they will buy back.

Actually, the only real question is at what price will the traders which have been buying from the managed money traders all the way down in price agree to sell to the managed money traders on the way up in price. That's also at the heart of my "big one" premise, as all the potential sellers (or at least JPMorgan) have to do is keep their hands in their pockets and not sell and prices will surely explode.

So not only have the managed money traders never won in the end when establishing big positions in gold and silver, when they establish big short positions, they are particularly vulnerable to losses. In fact, the only way the managed money traders could win now is if the commercials somehow panic and sell most or all of the contracts they have bought on lower prices from here. Considering the commercials have been killing the managed money traders all along, that seems more than unlikely. I guess one never wants to say never, but the commercial now losing seems farfetched to the extreme. The opposite of farfetched is a sure thing.

Can I tell you when the managed money traders will be done selling to the downside and when they will start buying back at higher prices? Of course not. But that's very different from stating that it's only a matter of time before they do both. The sure thing is not predicated on a precise time or price; it's based upon what is most certain to occur. I've admitted upfront that the only variable is how many more contracts the nitwit managed money traders may sell, which neither I nor anyone else can pinpoint in advance. But based upon historical parameters and trading activity, we would seem to be close enough for all practical purposes. It's against my religion and age to hold anything on margin, but as far as being all in on a cash on the barrel head basis and being loaded up to the gills on out of the money call options – you betcha.

As far as Friday's COT report, as I've already indicated above, I would expect significant managed money selling and commercial (and other large non-commercial) buying in gold, largely as a result of yesterday's trading, although I always fret whether big changes on the cutoff day will make it into the report on time. But it's also important to recognize that if the trading did take place but hasn't made it into the report on time, who cares? Much more important is that the trading that took place, not whether it's reported on time. I would imagine it will be a big number in gold, say 30,000 net contracts of managed money selling or more, but even if the number is less than that, I wouldn't be particularly concerned as a lower number could still indicate an exhaustion of managed money selling.

Silver's a bit different in that there seemed to be aggressive managed money selling yesterday, but there looked to be managed money buying earlier in the reporting week as the 200 day moving average was challenged to the upside. I'd venture we had net managed money selling for the reporting week in silver, but the market structure in silver has been extremely bullish for so long that it's starting to look permanent. Don't let that fool you. A few weeks back, I mentioned that gold's market structure had moved into the bullish state, perhaps providing a link that had been missing in accompanying the extremely bullish market structure existing in silver for some time. At this point, both gold and silver are now structured as extremely bullish and in the terms I've always found to be most important for price, both seem aligned for an upside move of some significance.

Ted Butler

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Silver – \$16.40 (200 day ma – \$16.81, 50 day ma – \$16.54)

Gold – \$1292 (200 day ma – \$1308, 50 day ma – \$1329)

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