

## May 7, 2016 – Weekly Review

### Weekly Review

Despite rallying on Friday upon release of the monthly employment report (for whatever reason), gold and silver finished lower for the week, with gold ending \$4 (0.3%) lower and silver lower by a more substantial 37 cents (2.1%). As a result of silver's relative underperformance, the silver/gold price ratio widened out by nearly 1.5 points to just under 74 to 1.

Four months into the year, silver has performed better than gold as a result of its relative outperformance over the past month or so, but it's closer to the truth to say that the price ratio is still stuck in a trading range extending back for more than a year. And while relative performance in the short term is still a tossup, closest of all to the truth is that silver is still bizarrely underpriced relative to gold on a long term basis.

I know I have grown quite repetitive in remarking how pervasive commentary on the Commitments of Traders (COT) Report has grown, but it is simply astonishing, as well as fully deserved. After yesterday's report, I expect even more pervasive commentary, given the dramatic (although expected) results in the gold COT report. Let me run through the usual weekly format first.

The turnover or physical movement of metal brought into or taken out from the COMEX-approved silver warehouses cooled off this week to just over 2.5 million oz., as total COMEX inventories rose 0.7 million oz to 152.7 million oz. Of much more interest was the 2.7 million oz withdrawal of metal over the past few days from the big silver ETF, SLV, which is as counterintuitive and unexpected as it gets. You'll remember that on Wednesday, I commented that the 4.1 million ounces that had come into the trust over the past week thru Tuesday was fully expected and overdue, given the trading volume and upward price path.

There is nothing about trading volume and price action that supports this recent withdrawal of silver from the SLV, particularly when considering the still large inflows of gold into the large gold ETF, GLD. Therefore, one must resort to alternative explanations of which I can uncover only the same two as always – the conversion of shares to metal to avoid SEC ownership reporting requirements and/or the removal of metal because it is more urgently needed elsewhere. Once plain vanilla investor liquidation is eliminated (as appears to be the case here), there are not many other explanations possible. Needless to say, if either one of my two plausible explanations is at play, the bottom line points to physical tightness in the wholesale silver market.

Speaking of physical tightness in silver, over the past week, the two major annual reviews of the silver market were released – the Silver Institute's review by GFMS (Thompson Reuters) and the review by the CPM Group. I'm not a big fan of either review (and find Jeffrey Christian of CPM a truly despicable human being), but both point to shrinking supply and growing demand. Both are supportive of higher silver prices on an actual supply/demand basis, but so what? Fundamentals have had nothing to do with silver prices, only COMEX positioning. Someday, of course, that will change. Remarkably, what hasn't changed is that the two reviews differ by more than 100 million oz in their calculation of annual world silver mine supply – the one feature you would think they would agree on (GFMS is at 885 million oz, CPM at 784 million oz).

Sales of Silver Eagles reverted to the sellout mode as the million ounces allocated (rationed) by the US Mint, plus the handful of coins not purchased by JPMorgan in the previous week(s) were snapped up and we hit the 20 million oz market for the year. I know the one million oz per week sold by the US Mint has become expected and thoroughly routine, but it is nothing short of amazing that so many Silver Eagles are being produced and sold; particularly considering that retail demand, except for temporary spurts, has continued to stink up the joint.

For the first 20 years of the Mint's American Eagle Bullion Coin program, now in its 30<sup>th</sup> year, the Mint rarely sold one million Silver Eagles a month, with many years half that rate. And no one even dreamed that the US Mint would be forced to ration Silver Eagles on a regular basis. Now, sellouts are expected and routine. But the strangest thing of all is still that the Silver Eagle sellouts have become routine without the presence of strong retail demand. It was this strange set of circumstances that led to my discovery and conclusion that JPMorgan was scooping up as much or more than 50% of all the Silver Eagles produced over the past five years. When I disclosed this finding a few years ago, many scoffed at my conclusion. But retail sales have mostly remained weak and actual sales of Silver Eagles have remained strong and as a result, the scoffing has subsided.

[http://www.usmint.gov/about\\_the\\_mint/index.cfm?action=PreciousMetals&type=bullion](http://www.usmint.gov/about_the_mint/index.cfm?action=PreciousMetals&type=bullion)

The May delivery process for both COMEX silver and gold still indicates physical tightness. In silver, JPMorgan has taken 826 (47%) of the 1757 contracts issued so far and with around 1050 May contracts still open and with JPM stopping contracts at a recent rate of close to 65% of new contracts issued, it looks nip and tuck as to whether the bank will get to the 1500 contract (7.5 million oz) limit allowed or if physical material has gotten too tight to demand the full amount, lest it influence silver prices. As in its buying of Silver Eagles, JPMorgan is only interested in buying as much physical silver as it can without causing prices to rise. Remember, we're talking about the master market criminal of the financial universe.

In gold, the number of May contracts still open remains stubbornly high at 1441, with only 632 contracts issued so far this month. May is not a traditional delivery month in gold and follows a tight April delivery process and precedes a traditional June delivery process where rollovers have already commenced. In gold, the Bank of Nova Scotia has been the big stopper, followed by JPM (all in their proprietary or house trading accounts). In silver, it's reversed, but both banks are thought to be the biggest shorts in each market, where one would normally think they would be issuing, rather than stopping deliveries. I suppose that would be normal only in non-manipulated markets.

[http://www.cmegroup.com/delivery\\_reports/MetalsIssuesAndStopsYTDReport.pdf](http://www.cmegroup.com/delivery_reports/MetalsIssuesAndStopsYTDReport.pdf)

On to the changes in the COT Report. On Wednesday, I tried to explain how I was more calculating rather than just guessing (based upon the existing extreme structure in gold and the big change in total open interest for the reporting week) in predicting we would see anywhere from a 30,000 contract to a 50 or 60,000 contract increase in the total commercial net short position. The actual numbers were at the upper end at nearly 55,000 contracts, one of the largest increases in history. (I took a pass on silver, which was just as well considering the mostly unchanged reported results).

In COMEX gold futures, the commercials increased their total net short position by an astounding 54,800 contracts to 294,900 contracts. This is one of the largest (most bearish) readings in history; last seen when gold approached \$1900 in 2011 and a few times in the years preceding that. Perhaps the most astonishing feature to the current extreme commercial net short position is how quickly we got to these readings compared to the previous extreme readings.

Quite literally, what formerly took years to develop has taken little more than a few months. It's hard to believe, but at year end, we were at or near historical bullish readings in gold and silver and I think that was fully reflected on these pages. Now we are at bearish extremes I didn't think was possible after only four months and a \$240 rally in gold and a \$4 rally in silver. I'll come back to this in a moment.

By commercial category in gold, the Three Musketeers must have been turning over in their graves as the COMEX commercials were swinging from the rafters and prancing up and down the castle steps. The big four added 24,300 new shorts, the 5 thru 8 big shorts added 14,800 new shorts and the raptors added 15,700 new shorts. There were a few times the concentrated short position of the big 4 and big 8 may have been slightly larger, but what could that matter?

On the buy side, it was mostly a managed money affair, as it usually is on big weekly changes, as the technical funds bought nearly 47,000 gold contracts, including 42,366 new longs and the short covering of 4479 contracts. Since we were already at managed money net and gross record long positions before this report, new high water marks were established. And don't look now, but the preliminary open interest for yesterday's gold rally indicates another sharp jump in open interest which, if not adjusted sharply lower on Monday, indicates the high water marks were reset much higher (and more bearishly).

I don't like to single anyone out (it's not professional generally) but among the explosion of COT commentary I observe daily was a piece by Bob Moriarty on 321gold crudely mocking some other COT analysis (not mine, but based upon my prior work). Anyway Bob stated flat out that small traders were responsible for COT commercial positions and changes and that the banks weren't involved much. Small traders involved and the banks not involved much? The COTs are nothing but banks and big managed money traders; small traders have next to nothing to do with the process. And what does he suppose the Bank Participation Report measures, if not participation by banks in the futures market. By the way, the percentage of market share held by the banks is extraordinarily large in COMEX gold and silver and other COMEX/NYMEX metals. Let me go on to silver, before coming back to gold and trying to put everything into perspective.

In COMEX silver futures, the commercials actually decreased their total net short position by a scant 700 contracts, to 90,600 contracts. The big 4 bought back 400 short contracts, the big 5 thru 8 added nearly 800 shorts and the raptors bought back nearly 1000 shorts, in stark contrast to what occurred in gold. As a reminder, both gold and silver surged by nearly the same percentage during the reporting week, but gold's advance of more than \$60 at its high seemed much more dramatic than silver's 75 cent gain. Certainly, this was reflected in the large increase in gold's total open interest, while silver's open interest fell over the reporting week.

While I was encouraged with the slight decrease in the short position in the big 4 category and increase in the big 5 thru 8 short category, as it kept alive my premise that JPMorgan might be double crossing the other commercials, I got no conclusive proof in the Bank Participation Report because both US and non-US banks increased their gross and net short positions in silver by roughly the same amounts over the month. It's possible and even likely that the Bank of Nova Scotia may have replaced JPM as the big silver short, but the data just aren't clear enough for me to declare that. So I must wait a bit longer for additional evidence.

There wasn't much to report on the managed money front in silver except that the gross long position was up by 1187 contracts to 81,012 contracts, another new record. Managed money shorts were up by nearly 4000 contracts to 12,646, so no new net long position record was established.

There is no doubt that both the gold and silver market structures are exceptionally bearish. Yes, it is true that both have been bearish for some time and yet prices have held firm and have nudged higher. But it's important to recognize that timing was never a hallmark of COT analysis. The COT analysis is about price and positioning, not timing. I still believe, although I may be proven wrong, that the commercials are in complete control. I also believe that if the commercials lose control, it will become obvious to all. That day is coming, although I don't think it's here just yet.

Along those lines, I'd like to rehash some things I've talked about in the past, but not recently. Having anticipated the massive increase in technical fund buying and commercial selling in gold this week, I can't shake the feeling that the commercials have orchestrated the price rise in gold and silver this year. I know that it takes buying to cause prices to rise and I also know that the commercials have been sellers, not buyers. Therefore, I am not saying the commercials caused gold and silver prices to rise, since the buying was done, mostly, by the managed money technical funds. Instead, I am saying that the commercials orchestrated the technical fund buying, so that the commercials could sell into that buying. Why do I say this?

For one thing, the commercial selling looks very sophisticated and professional. The technical funds are conditioned to buy as prices rise and sell as prices fall (especially when moving averages are penetrated) — that's just how technical traders operate. I know this, you know this and, most of all, the commercials who trade against the technical funds know this. But more than just knowing it, the commercials have some extraordinary advantages in inducing the technical funds to buy (or sell).

Last week, I mentioned how the commercials, after booking close to \$750 million in realized profits on the run up in gold and silver prices this year, had assembled a large net short position in gold, 240,000 contracts or 24 million ounces, at an average price of around \$1240. As a result of the \$50 run up in gold prices last week, the commercials were behind or held open and unrealized losses of \$1.2 billion (and more when silver is added in). Most of the commercial short position in gold and silver is highly concentrated, meaning that the bulk of the position and open loss are held by the 4 and 8 largest traders. This is about the largest open loss the commercials have held in my recollection.

This week, the commercials added another 55,000 short gold contracts through the Tuesday cutoff and more, undoubtedly, on yesterday's rally. So let's be ultra conservative and keep it simple and call the total commercial net short position at 300,000 contracts or 30 million oz of gold. Remarkably, even though the commercials added to their gold short position impressively, they did so only after gold rallied sharply and incurred no additional mark to market open loss, by my calculations. In other words, the commercials increased their net short position in gold by 25% in little more than a week, but because they did so only after gold rallied sharply, they incurred no additional open losses.

I believe the commercials can handle additional open losses on a temporary basis, but this week they were able to increase their net short position without having to do so, with the net effect of increasing the average price at which they are short 300,000 contracts by ten dollars or more to \$1250 or higher. Conversely, the technical funds increased their net long position by the same 50,000 or 60,000 contracts, but at the cost of increasing their average buy price by ten dollars to \$1250. This is what I mean by the commercial selling looking very sophisticated and professional — they increased their short position with no out-of-pocket cost or increase in open loss and significantly improved their average selling price.

Yes, it is unequivocally true that from this point forward, should gold prices rise, it will cost the commercials (and benefit the technical funds) \$30 million for every one dollar gold rises and \$3 billion for every \$100 that gold rises in price. At its core, this is like a giant poker game and the pot has never been larger. To my mind, this is the most the commercials have ever been in the hole (in terms of unrealized losses), so one could say it is do or die for the commercials. But I'd be lying if I said I thought this was an honest and aboveboard poker game. It's much closer to the truth to say COMEX gold and silver is the most crooked poker game ever. It goes back to the advantages the commercials hold. What advantages?

Like dealing with marked cards or from the bottom of the deck, the commercials hold advantages few are aware of. For one thing, every commodity trader from a managed money technical fund dealing in thousands of contracts to a mom and pop retail investor dealing in onesie's and twosie's, must do business through a COMEX clearing member firm, either directly or through another brokerage intermediary. Guess who the clearing members are? Correct, the commercials, with JPMorgan being the largest. No one knows the financial circumstances and wherewithal and trading intentions of a brokerage customer better than that customer's broker. The clearing broker has to know these things, because if it doesn't it could end up with the customer owing the clearing broker tons of money. (As a former broker, I can assure you that the very worst thing that could happen to a broker is to end up with an unsecured debit as a result of a customer's bad trades and inadequate finances).

What, you say this is crooked as all get out for a bank like JPMorgan to have intimate financial knowledge of its customers and to be able to deal directly against those customers? Welcome to how commodity business is transacted. As an independent analyst, I have to try to determine the extent that the technical funds can buy or sell based upon public data and past behavior. As a clearing firm, JPMorgan and other banks and prime brokers have more than intimate knowledge about every one of their customers, probably better than the customers know themselves.

As I've tried to point out over the years, gold and silver prices bottom out when the technical funds have exhausted their ability to sell and prices top out when the technical funds have used up their collective buying capacity. You and I have to guess when that is, based largely on past history. JPM, et al, don't have to guess because they know, likely even before the technical funds themselves. You say that's worse than a crooked card game featuring marked cards and dealing from the bottom of the deck and you expect me to disagree? Throw in the ability to fix prices via crooked HFT computer programs and a federal commodities regulator no more effective than a piano player in a whore house and a crooked card game starts to sound like a Sunday Bible reading.

But this isn't just a crooked card game with many billions of dollars in the pot; this is a congressionally authorized and federally regulated market that determines gold and silver prices for everyone throughout the world. In this sense, you can't quit the game or not play if you are a producer or consumer of any type, no matter how far removed. That's what makes price manipulation the worst market crime possible and what shields me from backlash from JPMorgan or the crooks at the CME.

I guess what I'm saying is that given the extent to which the commercials (mostly banks) are exposed on the short side and the technical funds are exposed on the long side and all the advantages and dirty tricks at the commercials' disposal, it will take an extreme black swan-type event to thwart the commercials. I would love to see it happen, but the highly sophisticated recent trading by the commercials, along with the unfair advantages they hold diminishes my expectations for a happy (upside) ending. That happy upside ending is surely coming, particularly in silver, but it's hard for me to see the commercials run out of Dodge City for cheating at cards just yet.

On the other hand, the moving averages have climbed enough since yearend that should the crooked commercials succeed in rigging prices low enough to induce significant technical fund selling, the price decline needn't be as deep as it once was. Because t

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