

## November 1, 2014 – Weekly Review

### Weekly Review

A brutal two-day sell off capped a week in which gold and silver fell sharply to new four year price lows. Gold ended \$58 (4.7%) lower, while silver was smashed for a full dollar (5.8%). Volume was extraordinarily heavy on the selloff, both in COMEX futures volume and in ETF trading. As bad as the selloffs in silver and gold were to metal investors, it was even worse for the shares of mining companies. Of course, to buyers the selloffs were nothing but good news.

As a result of silver's sharper percentage decline, the silver/gold price ratio widened out to 72.5 to 1 by the close, but had traded over 73 to 1 for much of Friday's trading day. This is also a 4.5 year low in the ratio and indicates extreme undervaluation of silver to gold. Since any value investor is primarily interested in acquiring assets at prices as far below value as is possible, the move to new lows in silver on an absolute and on a relative basis compared to gold means silver is a better value than any time in 4.5 years. While I have stated (and proven) that I can't predict the short term, I believe we will look back at current prices disbelieving silver ever got this cheap.

A few words on the brutal two-day selloff and what I have read as to its cause – basically Thursday's decline was due to the Fed's ending of QE and Friday's decline was due to Japan's acceleration of monetary ease. I don't mean to be disrespectful of others' opinions, but those explanations were contradictory and nonsensical. Let me see if I can't back up my assertion.

Gold and silver declined sharply for one reason only – technical fund selling on the COMEX. Of course, we'll have to wait until next week's Commitments of Traders Report (COT) for confirmation (and barring a sharp rally on Monday and Tuesday); but there has been massive technical fund selling on every price decline in gold and silver for months and years. In fact, there never has been a significant decline in the price of gold or silver without technical fund selling (and commercial buying). Based upon history and the basics of how technical funds operate – selling on price declines and buying on rallies – and considering that new multi-year price lows are the strongest sell signal possible for technical funds, there is little question that the technical funds (in the managed money category of the report) were the big sellers Thursday and Friday.

So what makes me say that the stories about the Fed or the Bank of Japan or anything else causing the sell-off were nonsense? It's simple. If the technical funds were the sellers as history and how they operate strongly suggests, then the central bank stories had nothing to do with the price declines because the technical funds never consider such things. The technical funds base their trading decisions exclusively on price movement itself and intentionally ignore stories and even supply/demand fundamentals in their price only approach. Therefore, if the big sellers in gold and silver on Thursday and Friday deliberately ignore the news accounts and solely focus on price, then to say that the selling was caused as the stories asserted is nonsense.

What's not nonsense is the effect that technical fund trading has had on the price of important world commodities, as those effects are all too real. A case in point is what effect the historic and unprecedented technical fund selling in COMEX silver has had on silver miners, particularly the primary silver miners. Should silver prices remain at current levels or move lower for an extended period of time, I doubt many, if any, primary silver miners would continue to exist. Certainly, the share prices of most silver miners seems to reflect this. While I do expect a sharp increase in the price of silver and soon, let's say I'm wrong and we don't rally hard.

What that would mean is that the technical funds (of which there are 40 in silver according to the latest COT report) succeeded in depressing silver prices low and long enough to put legitimate mining enterprises out of business. And while no commodities are as artificially depressed as is silver, this technical fund pattern is obvious in many commodities operating under the CME Group exchange umbrella, including gold, copper, platinum, palladium and crude oil. A subscriber asked this week about corn and other grains. I looked it up and it's the same there as well, namely, that the traders in the managed money category always account for the largest amount of selling on declining prices and always register the largest amount of buying on rising prices of any other group of traders.

This is the clearest proof that all our regulated futures markets are being manipulated by excessive speculation in the managed money category. Since it would seem impossible for the regulators (CFTC and CME) not to be aware of this that leaves only criminal involvement as an explanation for why they allow it to continue. Further, since managed money trading may be the single biggest source of revenue to the CME Group, there is a built in incentive for the CME to look the other way. What's the incentive for silver mining companies to also look away? I've got no answer to that question.

Turnover or movement of physical metal into and out from the COMEX-approved silver warehouses cooled, but only slightly this week as more than 4.1 million oz were shuffled from trucks to warehouses to trucks. Total COMEX silver inventories fell more than 600,000 oz to 180.5 million oz. I continue to maintain that this unprecedented and frantic physical silver turnover over the past three and half years is due to an underlying tightness in the wholesale physical silver market. Further, I've come to believe the reason no alternative plausible explanations have emerged is because none exist. I'm still noticing a pick up in COMEX gold warehouse movement and if that gold turnover continues, maybe it will help focus attention on what has been going on in silver for a long time.

There was a deposit yesterday of almost one million oz in the big silver ETF, SLV, but I'm not sure if that fully-reflected Thursday's and Friday's high volume trading. I don't know what to expect in terms of SLV deposits or withdrawals and instead still marvel at the stark contrast in the metal holdings of SLV and the big gold ETF, GLD. On very similar price patterns since the start of 2013 (down for both) GLD holdings are down by 19 million oz or nearly 45%, while SLV holdings are unchanged to a bit higher and remain close to all-time highs. I wouldn't think of selling silver and perhaps the holdings in SLV suggest that for others as well.

The US Mint issued a blockbuster of a sales report for Silver Eagles for October with nearly 5.8 million coins sold. In the 28 year history of the American Eagle Bullion Coin Program, sales have only been higher in three other months. All three of the months in which Silver Eagles have been higher were in January, when the Mint usually reports the heaviest sales of the year as a result of retooling and beginning to produce coins earlier to reflect the New Year. In other words, if you eliminate January's sales due the extra production profile, this October's sales were, effectively, the largest "regular" month in history.

[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)

While retail silver demand picked up noticeably on the price swoon of the past two days, in my experience that increase in retail demand would not be reflected in yesterday's report from the Mint as it takes time (days) for retail demand to trickle up to the wholesalers which buy directly from the Mint. I'm still convinced, therefore, that a single big buyer (you know who) has accounted for much of the surge in Silver Eagle sales over the past three months. This surge came after a notable dip in sales in the previous three months.

I've speculated that JPMorgan was the Mr. Big buyer in Silver Eagles and in SLV and recent data reaffirm my guess. And considering the production capacity of the US Mint, it appears to me that Mr. Big may have completed the purchase of most, if not all the extra Silver Eagles the Mint produced but didn't sell when the big buyer stepped aside from June thru August. Why should JPMorgan have bought heavily when it knew silver prices would be lower soon and it could save many millions of dollars by delaying its purchase of Silver Eagles until after prices dropped? After all, the many millions of dollars came out of US taxpayers' pockets, so no big deal. Isn't this what JPMorgan exists for?

There were no big surprises in this week's COT report, but none were expected, as prices for gold and silver were fairly flat to lower on subdued trading volume during the reporting week. Of course, all eyes will be on next week's report which will reflect the dramatic declines since the Tuesday cut-off. In last week's review, I had expected some technical fund selling/commercial buying in gold, following two weeks of strong fund buying and commercial selling.

In COMEX gold futures, the total commercial net short position declined by 6100 contracts to 98,900 contracts. You'll remember that the commercials had sold more than 41,000 net gold contracts on the \$60 gold price rally over the previous two reporting weeks and I had opined how that increased the chance of a sell off to draw back to the sell side those technical funds who bought on the rally. After Thursday and Friday, I would guess the gold technical funds did sell and the commercials have now repurchased all gold contracts they previously sold and the market structure is back to extremely bullish as a result.

By gold commercial categories, the 4 big shorts actually added nearly 3000 new short contracts, with the big 5 thru 8 shorts buying nearly 2000 short contracts back. This left the raptors as the big buyers or 7000 contracts. After weeks of selling by JPMorgan, the bank appears to have added 2000 contracts to a long position now amounting to 18,000 contracts.

There was less net selling by the technical funds than the commercial bought, as managed money traders sold around 2400 contracts on balance, including a nearly 2000 contract reduction in the all-important gross short position. With more than 68,000 contracts held short in the managed money category, I would imagine, given that Thursday and Friday triggered an impossible to ignore sell signal to a technical fund, that managed money shorts are back to 80,000 contracts short and maybe even at a new record above 83,000 contracts. The rocket fuel tank of technical fund short covering would appear to be topped off, or nearly so.

In COMEX silver futures, the total commercial net short position declined to another new low dating back to the beginning of last June, but only by 400 contracts to 14,200 contracts. The big 5 thru 8 short holders bought a few hundred contracts back and the raptors increased their net long position by 1000 contracts to 42,400 contracts. The big 4 were short sellers of 750 new contracts and, accordingly, I'd mark up JPM's short position to 12,500 contracts, although I suspect it might not be JPM as the big seller in the big 4 category. Next week's Bank Participation Report may help clarify things further.

The good news on the sell side of silver was that the gross short position in the managed money category increased by more than 1100 contracts to more than 46,000 contracts, another new record. I did an interview with Chris Martenson from Peak Prosperity yesterday before the new COT report was issued and he was taken back a bit when I told him that the technical fund short position was at a record level and he asked me a couple of times to confirm that it really was at an actual record. Chris mentioned that he always paid attention when any reading was at a record level and later concluded (with no direct prompting from me) that he intended to buy more silver forthwith. When I get a link to the interview, I'll pass it along.

I would imagine that the technical fund short position is now at dramatically higher new record levels as a result of the price pounding since the cut-off, perhaps by 5000 contracts or more. Since I had felt that the rocket fuel tank was already topped off in silver; I now feel the equivalent of supplemental tank capacity has been added and filled. In fact, I believe that Thursday's and Friday's trading action has, if anything, accelerated the resolution dead ahead and added markedly to the explosively bullish set up.

Based upon the futures contract positioning of the technical funds and the decline in the price of silver over the past three months, I would now calculate that the technical funds are now sitting on a \$600 million open profit (roughly a \$3 profit on 40,000 short contracts added since mid-July). This is, by far, the largest open profit held by the technical funds in COMEX silver, long or short. The question has been asked and underlined this week "Will they keep it?" I still say they won't, but that will be decided in the near future.

A number of subscribers have asked about the ability of the long holders to withstand the crushing losses inflicted on them as a result of the brutal price drop on Thursday and Friday. No doubt many long futures holders were forced to sell, most likely from an inability or unwillingness or hesitancy to come up with new margin money demanded by their brokers. But it would appear that the biggest long holders, namely, those in the managed money long category (not technical funds) and the commercial raptors likely held firm and added positions.

The raptors, for instance, have been adding to their now formidable net long position since July on declining silver prices and just this week hit their largest net long silver position since then. I suppose it's possible some of the raptors may have turned tail and sold on the big decline this week, but I don't recall that ever happening and I will only believe it when I see it. The raptors are commercials and as such, don't have margin limitations or problems. If I had to bet, I'd wager the raptors added long positions on the sell off for the simple reason that I believe they were the architects of the price smash (along with JPM).

The bottom line is that the sharp selloff has only strengthened an already extreme market structure by adding new technical fund shorting, the flushing out of under-margined longs, further short covering by JPMorgan and new raptor buying. While I consider this extremely supportive of higher prices to come, there is also a very ugly side to this as well. Because the mechanical machine trading of derivatives by the technical funds is exclusively responsible for the setting of prices for almost all important commodities, it is causing havoc in the real world of commodities.

Nowhere is this more visible than in the plight of the primary silver miners. Most of these miners have been reporting losses or marginal profits at silver prices several dollars an ounce higher than current prices; meaning that if we don't rally sharply (as I expect) these miners appear doomed. How long can a resource producer continue to produce at a loss, especially following years of an eroding financial position? Forget about how long before silver production reflects this – the more important point is that the primary silver miners are suffering now; and for no legitimate reason, unless one believes the technical funds (and commercials) are on solid ground in setting prices for the world's producers and consumers. I say that's nuts and here is where I end up calling the CME crooked for encouraging it.

But instead of stopping there, let me offer a constructive suggestion for the silver miners to fight back against a price manipulation that threatens to put them out of business. Further, the suggestion is easy, cost effective and does not involve illegal acts of price fixing among producers.

What the silver miners or a single miner (for instance, First Majestic) can do is to write to the all the regulators (but certainly including the CFTC and the CME) about the technical funds undue influence in setting silver prices and, most importantly, make that letter as public as possible, including placing it in selective publications. Care must be given to include only the strongest of facts and not the usual whacky allegations, but fortunately as you may know, those facts already reside in COT data.

For years, the CFTC has held that allegations of manipulation in silver are not legitimate because no producer has ever complained. So here's a chance for a miner or group of miners to speak up instead of being bled to death by the speculators on the COMEX. This suggestion may be unnecessary and even too late if my expectations play out in silver sharply rallying; but it certainly is not only doable and logical, but also hard to imagine why it shouldn't be tried.

We are at what appears to me to be an historic junction in silver; almost the mirror image of the position silver was at the top in 2011. I think physical market conditions currently are as tight as or tighter than what existed in April 2011, but all other conditions are markedly different. Back then, JPMorgan and the commercials were not positioned for a sharp rally that's why they fought it (and succeeded). Today the commercials are better positioned (save for the other 7 members of the big 8) on the COMEX than ever before. In the May 3, 2011 COT report, the technical funds were short 5000 contracts compared to the nine or ten times more they hold today. Back then, JPMorgan was only deciding to build up the massive long physical position I believe it holds today.

Finally, back then there were many investors holding silver strictly because it had gone up so much in price and were, therefore, in a position of being forced to sell on suddenly lower prices (which occurred). Today, only the battle-scarred remain and there are few, if any, investors holding silver because the price action has lured them into buying something for the simple reason it had gone up. I could probably come up with more differences, but how many do you need?

Ted Butler

November 1, 2014

Silver – \$16.20

Gold -\$1173

**Date Created**

2014/11/01