November 23, 2016 – Will They or Won’t They?

Will They or Won't They?

Of course, I'm referring to the question of whether the managed money traders will add aggressively to short positions in COMEX gold and silver futures from this point on lower prices. That was one of the two standout features in Friday's COT report, namely, the very light short selling by these technical fund traders on what was a very dramatic down reporting week (the other being the aggressive short covering by the largest commercial shorts). I've been thinking deeply about this since the report's release and judging by the many comments and questions from you, I'm not alone.

To be sure, it wouldn't seem prudent to rely on just one week's report to proclaim a major paradigm shift in technical fund behavior had occurred. Perhaps there was some type of serious reporting error to account for the lack of aggressive managed money shorting and that will soon become obvious in future COT reports (the next one being the holiday-delayed report next Monday). Perhaps the technical funds intend to sell short on even lower prices (although that is hard to rationalize). But barring a large reporting error and/or a dramatic increase in managed money short selling in future reports, last week's report is still center stage in my mind. And to my knowledge, the unusual phenomenon of the lack of managed money short selling has not been independently commented on elsewhere, making it something overlooked.

Let me first discuss why this development is so important to me and then I'll touch on how it might have come about. It has to do with the Â?countÂ? Â? the amount of managed money buying or selling I've used to identify price tops or bottoms in gold and silver over the years. After the managed money traders buy as many contracts as they have in the past (or even more) that generally signifies we are close to a market top. Conversely, after the managed money traders have sold and sold short as many contracts as they have historically that represents a bottom in terms of the market structure premise that I adhere to. Price and time are subservient to the actual number of contracts positioned.

If the managed money traders have, for whatever reason, altered their behavior and collectively decided not to add the same number of contracts to the short side of COMEX gold and silver that they have typically added in the past, then that would directly alter how the Â?countÂ? is measured. Let me give you an example of what I'm talking about in silver. On four separate occasions from 2014 through the end of 2015, the gross short position of the managed money traders totaled more than 40,000 contracts; with the peak in managed money shorting roughly occurring at price bottoms. On the most recent occasion of peak managed money shorting on Dec 15, 2015, these traders were short right around 48,000 silver contracts.

In last week's COT report, the managed money traders held a gross short position in COMEX silver futures of just over 16,000 contracts or close to 32,000 fewer contracts than on December 15, 2015. This despite the fact that the price of silver plunged sharply in the latest reporting week, decisively penetrating the 50 and 200 day moving averages on very high volume, typically a clear cut invitation for technical fund short selling. Accordingly, last week's report was of the shocking variety because the managed money traders hardly added to silver short positions.

Strictly on a mathematical basis, if the managed money traders have, in fact, radically altered and reduced the number of new short contracts they intend to sell in silver, then the contract count indicating a price bottom must also be altered by the reduced amount of contracts they intend to sell short. For example, if the technical funds intend to sell short silver contracts to the tune of 20,000 or 30,000 contracts less than they did at the previous peak last December, it would be unwise to expect or wait for them to do so.

In other words, if (perhaps a big Â?ifÂ?) the managed money traders don't intend to sell short in the quantities they've previously sold that should result in an Â?all clearÂ? signal, by contract count, arriving earlier than previously Â? or a buy signal with a higher commercial net short position higher than previously. In addition, as I mentioned on Saturday, there is a mechanical aspect to this. If the technical funds are not going to add to short positions as they have in the past, there is that much less for the commercials to buy (and cover their short positions).

According to the way I see things, prices in silver and gold mostly move based upon how the commercials are maneuvering the managed money traders. Neither real supply/demand considerations nor much of anything else dictates price movement Â? just COMEX futures positioning. The commercials are solely interested in making money and the only way they can make money in COMEX futures trading is to get the managed money traders to buy high and sell low Â? which the managed money traders are inclined to do anyway as technical-type traders.

The amount of money the commercials make is directly proportionate to the amount of money the managed money traders can be persuaded to lose. This year, as I have chronicled, historically large managed money buying in COMEX gold and silver futures on continually rising prices into the summer resulted in open (not realized) gains of $4 billion to the technical funds and the same amount of unrealized losses to the commercials. This was the most the technical funds had been ahead and the most the commercials were in the hole ever in gold and silver.

With today's sharp price decline and the price decline since the summer highs, I would estimate the managed money traders have lost completely their $4 billion open profit and have flipped that into a $4 billion loss. Likewise, the commercials have gone from being $4 billion behind to $4 billion ahead, with much of the technical funds losses and commercial gains now booked and realized. This is the greatest financial turnaround in COMEX gold and silver history and I can't claim that I am surprised that the commercials came out ahead, since I have always contended that they are in control.

Today's sharp price decline raises to a new level the question of whether the managed money traders are now adding aggressively to short positions in COMEX gold and silver. There is no question, of course, that today's sudden price plunge is solely due to the commercials rigging prices lower to induce managed money selling, both long liquidation and new short selling. The question is how much new short selling is occurring. To be frank, I don't know. I do know that Monday's COT report will not reflect today's positioning, since yesterday was the cutoff for that report. I can only wait for Monday's and future reports to know for sure. I suppose that's better than waiting for years.

I'll return to today's action after commenting on why the managed money traders may have collectively decided not to pile onto the short side in gold and silver now as heavily as they have in the past. This was a feature of many of your questions Â? why now? Alternatively, perhaps the question should be Â? what took them so long? Aggressively adding to short positions in anything at severely depressed prices is not one of the golden investment rules and the more volatile the commodity, the less appealing the practice would seem to be.

Yes, I know that Â?severely depressedÂ? is a subjective term, but there is a long history (decades) of the managed money traders being behind the eight ball and coming up losers when shorting gold and silver heavily. Compare the managed money traders' experience of shorting gold and silver over the years of rarely winning to the commercial shorts' record of rarely losing. Over the decades that I have observed COMEX trading results and reported on those results, the question on my and many others' minds is why do the managed money traders persist in such folly? The answer is that maybe they finally woke up to realization that when they go heavily short COMEX gold and silver, the managed money traders generally prevail very poorly.

As to how this realization may have come about, I would point out that the managed money traders collectively hold hundreds of billions of dollars of investor assets, which makes them significant financial institutions in their own right. As such, the managed money traders have their own organizations which advances an agenda intended to benefit their own industry, same as any industry. There's even a Managed Futures Association which does just that.

https://www.managedfunds.org/

What I write about has everything to do with the commercials snookering the managed money traders and it would be fair to characterize my running description as institutional fraud against the interests of the managed money traders. It is precisely what an industry association should be interested in. Would it be so hard to imagine an industry association examining the issue and for many of its members to choose to stop being put in harms' way by continuing to sell short gold and silver in the hole? I'm not stating they got the idea from me, although it is possible. The important point is that the managed money traders, for whatever reason, may have woken up to the fact that good things don't usually happen for them when they all short gold and silver heavily.

We'll know fairly soon if there has been a sea change in the managed money traders' inclination to go short gold and silver in upcoming COT reports. I would expect some increase in managed money short positions based upon the price action through today, but will readily admit that if these traders finally resort to the full and heavy shorting of the past, then the last COT report was a false alarm or that I read it all wrong. The jury will come in on that verdict fairly soon.

Even if the lack of managed money short selling in the last COT report was a fluke and false alarm, in that they did subsequently revert to shorting heavily once again, all is not lost for a coming rocket ride up in silver and gold. In fact, if today's selling does involve heavy managed money short selling that would just add to the reserve of short covering Â?rocket fuelÂ? to be expended whenever prices do turn upward. There's no question that lower prices sting and hurt as far as the value of existing positions, but those same low prices aid tremendously in resolving the market structure. I know, I know Â? enough with the resolution of market structure, just make prices go up already.

I have become very bullish as of late and as much as I wished I had waited a bit longer (at least until today) to get as bullish as I am, today's rotten price action does nothing but strengthen the bullish structure. Could we get even more price pain from here? Of course, but such price pain will only make the structure even more bullish. The only, and I must empathize, the only reason for today's price smash was to allow the commercials to buy as many COMEX gold and silver contracts as possible. It was a COMEX price rig job as clear as any have been before it and must be recognized as such.

Further, today's sudden and intentional price smash actually raises the issue of whether the managed money traders will add heavily to short positions to greater significance. Today's fresh price lows were climactic in nature, with gold knifing to lows not seen since February. Considering how much trading has occurred below the important moving averages recently, accompanied by the succession of new price lows, it's hard to imagine how a technical fund could still be holding long positions and not having added to short positions by now. If they haven't sold by now, what the heck are they waiting for?

Guessing important price lows is always tricky business and akin to catching falling knives and I have the scars to prove it. But I feel strongly that this will be a price area we will look back upon as extraordinarily cheap. And I'm also still expecting that when we do turn upward, the trajectory of the advance will be much sharper than most expect for exact same reason driving this decline Â? it will be to the commercials' advantage (at least JPMorgan's) not to sell aggressively on the coming advance.

Due to holiday travel commitments, I'm ending this report early (noon EST). I plan on a Saturday review, but there will be no COT commentary in that review until Monday. Please accept my wishes to you and yours for a Happy Thanksgiving.

Ted Butler

November 23, 2016

Silver – $16.35 (200 day ma – $17.64, 50 day ma – $18.09)

Gold – $1188 (200 day ma – $1282, 50 day ma – $1277)

Date Created
2016/11/23