October 5, 2019 – Weekly Review

After starting the week down by more than $35 in gold and 60 cents in silver and far below the 50 day moving average in each, by weekâ??s end gold was up by $6 (0.4%), while silver managed to finish unchanged. As a result of goldâ??s slight relative outperformance, the silver/gold price ratio widened by a fraction to 85.8 to 1 (yet another week of mind-boggling undervaluation for silver).

At the price lows early in the week, the 7 big commercial shorts in COMEX gold and silver had managed to reduce their open and unrealized combined loss to under $3 billion for the first time in two months, but by weekâ??s end, the total open loss actually increased by $100 million to $3.7 billion at yesterdayâ??s close.

Aside from the volatile price action, the weekâ??s biggest development was yesterdayâ??s Commitments of Traders (COT) report, which indicated substantial and mostly expected managed money selling and commercial buying in gold and yet another surprise in silver where the managed money selling came in far below my expectations. Much more on this in a bit, after reviewing the usual weekly developments.

The turnover or physical movement of metal either brought into or removed from the COMEX-approved silver warehouses surged this week to 8.5 million oz, the largest weekly movement in more than 8 months. Total COMEX silver inventories rose by 2.1 million oz to 315.1 million oz, a couple of million oz less than the record set two weeks ago. Interestingly, despite the surge in movement this week, there was no change in the JPMorgan COMEX warehouse for the fourteenth week in a row (still stuck at 153.8 million oz).

This weekâ??s surge in physical turnover in the COMEX silver warehouses is the annualized equivalent of more than 50% of total world annual mine production and nearly double the average weekly movement of the past 8.5 years (since April 2011). No other commodity has anywhere near as active a physical warehouse turnover â?? the turnover in the COMEX silver warehouses is as unprecedented as it gets. Yet you can count on one hand (with a few fingers left over) the number of commentators even mentioning this highly unusual physical silver movement. And forget about any attempt to explain why the physical movement is occurring. For my part, I hold the movement reflects an extremely tight physical situation in silver and, moreover, that the turnover was created by JPMorgan in order for the bank to skim off more physical silver for its vast holdings.

Turning to gold, the October COMEX deliveries continue to be of interest on a number of fronts. Usually, October is the slowest of the traditional COMEX delivery months, but not this year. Already, the gold deliveries this month are the second largest of the year and five times greater than last Octoberâ??s deliveries. Even more interesting is that JPMorgan has been the largest stopper this month, taking 4002 gold contracts (400,200 oz) in its own propriety trading account, while customers of JPM have been the biggest issuers with 4645 gold contracts issued. By the way, to this point, a total of 10,390 gold contracts have been issued or reissued this month.

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

This gives the appearance of JPMorgan taking advantage of its own customers. As you may recall, the Justice Department, in its recent criminal indictments against JPM traders, pointed out that

JPMorganâ??s own customers were harmed by the spoofing of its traders. Hey, a bank has got to make money any way it can these days, so why should ripping off customers be exempt? By the way, 57,500 oz were moved into the JPMorgan COMEX gold warehouse yesterday, hinting at more to come given the large stoppings this month.

As a reminder, in addition to claiming that JPMorgan has amassed 850 million oz of physical silver over the past 8.5 years, I also claim that the bank has accumulated 25 million oz of physical gold. On a monthly basis, that comes to around 250,000 oz per month. This month, by virtue of the October COMEX deliveries alone, JPMorgan has picked up 400,000 oz, dispelling any suggestion it is finished with accumulating physical gold (or silver).

Other standout features in the October COMEX gold deliveries include HSBC issuing 4000 contracts from its house account and Macquarie stopping 2574 contracts for its house account. Other stoppers include Citibank with 1101 contracts in its house account, although every other time Citi has been a stopper of gold, it has turned around and redelivered all of what it stopped Â the same month. Goldman Sachs has stopped 1578 gold contracts this month in its house account, but has already redelivered 1034 contracts.

Normally, I donâ??t dwell on the details and intricacies of the delivery statistics, but the October deliveries seem to strongly suggest quite a tug of war for physical gold supplies above and beyond what is usually seen. Itâ??s much quieter in silver, as customers of JPMorgan have stopped 790 silver contracts, or a mere 86% of the 914 total contracts issued.

Things have quieted down in physical metal deposits/withdrawals in the worldâ??s leading ETFs (exchange traded funds), particularly in silver. To my mind, this cements the premise that a single big buyer picked up 100 to 125 million oz of silver a while back, first by buying COMEX futures contracts and the converting those contracts into shares of ETFs, principally SLV.

Turning to yesterdayâ??s COT report, I may have been expecting even more of a positioning change in gold than was reported, but was definitely expecting much more of a positioning change than was reported in silver (no, Iâ??m not deliberately trying to embarrass myself with my predictions). While I was way off in silver and, quite frankly, disappointed at first, laying out what happened and what is likely to happen from this point is more meaningful than a bruised ego. Let me cover gold first before analyzing silver.

In COMEX gold futures, the commercials reduced their total net short position by 41,500 contracts to 303,700 contracts. While I expected an even larger reduction, this reporting week was the largest reduction since April and the total commercial short position is the lowest since July 30. Importantly, there was a significant reduction in the concentrated short position of the largest traders.

Iâ??d estimate JPMorgan reduced its gold short position by 10,000 contracts to 45,000 contracts and the 7 big shorts (excluding JPM) are net short 210,000 contracts (21 million oz) as of Tuesday. As far as whether the big shorts closed out short positions at a loss (JPM certainly didnâ??t), since they added shorts into the top of gold prices and bought back lower, Iâ??m going to bypass the issue now and have already incorporated it into my running totals for open losses (above).

The managed money traders sold 47,060 net gold contracts, consisting of the sale and liquidation of 45,518 long contracts and the new short sale of 1542 contracts. The resultant managed money net long position is now (as of Tuesday) 190,811 contracts (219,990 longs versus 29, 179 shorts) and must still be considered bearish in conventional historic terms.

In COMEX silver futures, the commercials reduced their total net short position by a scant 2000 contracts to 73,800 contracts, causing me at first to utter something Iâ??ll not repeat here. The amount of managed money selling was greater, but not significantly in the broad sense of what I was expecting. It was the lowest commercial short position, since Aug 20, but that seemed like small consolation. Based upon the Bank Participation report and the changes in the Producer/Merchant category, Iâ??d peg JPMorgan silver short position to be 22,000 contracts (110 million oz).

The managed money traders sold 4731 net silver contracts, comprised of the sale and liquidation of 3553 long contracts and the new sale of 1178 short contracts. The resultant managed money net long position of 44,203 contracts (73,193 longs versus 28,990 shorts) must still be considered bearish on a historical basis and still much less bearish than the same position in gold (despite this weekâ??s bigger flush out in gold).

While I was disappointed when I first viewed yesterdayâ??s report, particularly in silver, my thoughts quickly turned to why there was so little managed money selling, considering the large price declines in gold ($70) and silver ($1.60) over the reporting week and the fact that the 50 day moving average was decisively penetrated in both markets for the first time in 4 months. It seems to me that the major resolution of the current market structure still lies ahead and will be one of two versions.

One version is the conventional resolution in which we will see a pronounced amount of selling yet to come from the managed money traders on successively lower prices (salami slicing). The world has come to accept the conventional COT market structure approach like never before for the very good reason that this has been a remarkably reliable approach. I would define conventional along the lines of what I have held for decades now, namely, as a game between the technical funds and their bank counterparties that happens to set prices.

So accepted has this COT approach become that I nearly gasped when I read the new report from the Silver Institute this week because the main focus was on COMEX positioning. Heck, if the Silver Institute is now talking about COMEX futures positioning, the only logical next step is that the COT market structure premise will be taught in public schools.

https://www.silverinstitute.org/wp-content/uploads/2017/05/SilverInvestment2019.pdf

Please understand that I am not and cannot knock the conventional COT market structure approach because that is the approach I taught myself over the past decades. Nor can I begin to certify that it wonâ??t turn out the same way it has always turned out in the past when the commercials have gotten heavily short and the managed money traders heavily long, like now. However, I must say that I generally become leery of any approach that comes to be accepted by nearly everyone, even one that I have pioneered. Iâ??d be lying if I said I wasnâ??t troubled that so many seem confident that gold and silver prices will be washed out to the downside by managed money selling that the commercials will then buy. I canâ??t say that wonâ??t happen, but I am bothered so many are counting on it.

Itâ??s not just that so many expect gold and silver prices to get flushed lower on managed money selling that bothers me; the actual mechanics of the expected managed money selling bothers me as well, particularly in silver. Specifically, there appears to a rather limited amount of managed money longs that can be liquidated on lower prices. As I mentioned above, the gross number of managed money longs is around 73,000 contracts. Before the rally began in late May, with silver prices around $14.25, the gross number of managed money longs was around 50,000 contracts.

Should silver prices truly collapse from here, therefore, it is unlikely we will see much more than 20,000 contracts or so of managed money long liquidation. And if any new non-technical funds have come into the market as a result of increasing attention to silver on a fundamental basis, then the number of longs to be potentially liquidated may be less than 20,000 contracts. That number of contracts is simply not enough, mathematically, to allow the big commercial shorts to buy back the bulk of their concentrated short position. It will take much more managed money selling in order for the big concentrated shorts to fully close out the bulk of their short position.

The only possible source of sufficient managed money selling that would enable the big commercial shorts to get out from under their big short position is new short selling by the technical funds (certainly, no one would advance the concept that any fundamental analysis of silver would warrant a big short position). So the real question is how many new short positions can the technical funds be tricked into putting on by the commercials? Thereâ??s no doubt that up until now, the commercials have been the masters of the technical funds. Iâ??ve used the example in the past of the commercials being the big grizzly bears feasting on the flow of technical fund salmon. While clearly dominant, if the salmon arenâ??t running, the bears wonâ??t eat.

Back on May 28, the managed money traders held a gross short position of roughly 88,000 contracts as silver traded down to $14.25. Thatâ??s close to 60,000 contracts more than the current gross short position of 29,000 contracts. If the commercials can hoodwink the technical funds into replicating the short position they held on May 28, the new short sale of 60,000 contracts or thereabouts would enable the commercials to buy back most, if not all of their big concentrated short position. The potential selling of 20,000 long contracts wonâ??t do it, but the new short sale of three times that amount would.

Again, the real question is whether the technical funds can be tricked into selling that many new short contracts? (By the way, the story is similar in gold, but silver is more stark). Unfortunately, Iâ??m better at asking these questions than in providing the answers because I donâ??t know what the technical funds will do. More succinctly, I donâ??t know how dumb these guys are. Never have the technical funds collectively exited a big short position in silver or gold with a profit. In fact, nothing accounts for a more bullish market structure than a big technical fund short position â?? with the most recent example being the price bottom on May 28.

One would think, at some point, the technical funds would wise up and avoid putting on big short positions in silver and gold that they have always lost on, but that could have been said for years and as recently as the time leading up to May 28. Technical fund short selling has never worked in silver or gold collectively, so itâ??s not unreasonable to imagine the technical funds would come to learn that as well â?? similar to one learning not to touch a hot stove after being burnt repeatedly. Then again, expecting the technical funds to have wised up prior to now would have been a losing bet.

While I canâ??t say what the technical funds will or wonâ??t do, I believe I have framed the equation correctly. If they do get snookered into going heavily short again, that will only occur on successive new price lows and the conventional COT market structure approach will have played out yet again, as is widely expected. However, if the technical funds donâ??t add aggressively to the short side, the widely-expected conventional outcome canâ??t occur and there will be a far different resolution.

Without massive new managed money short selling in silver, the big concentrated commercial short position canâ??t get bought back on lower prices, only higher prices. And based on the same market mechanics as described above, if, as and when it dawns on the big commercial shorts that massive new technical fund shorting is not going to bail them out, panic may set in. Again, Iâ??m not in position to tell you whether the technical funds will short or not, but that is what will determine prices ahead.

Right or wrong, this is definitely not part of any market structure analysis Iâ??ve come across. Neither is any discussion on how JPMorgan has put itself in position to double cross the other big commercial shorts due to its massive physical metal holdings. Be that as it may, thatâ??s the way I see it. If the nitwit technical funds add aggressively to short positions that will only occur on substantially lower prices, after which silver will be the all-time bargain investment. If they donâ??t add aggressively to short positions, it is hard see how or why silver prices would go lower at all and will likely explode higher at some point. Itâ??s imperative to be prepared for both resolutions.

Ted Butler

October 5, 2019

Silver – $17.60Â Â Â Â Â Â (200 day ma – $15.84, 50 day ma – $17.57)

Gold – $1510Â Â Â Â Â Â Â Â Â Â (200 day ma – $1366, 50 day ma – $1507)

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