
September 14, 2019 – Weekly Review

Gold prices fell for the third week, ending lower by \$20 (1.3%), while silver fell for the second week, ending lower by a sharper 65 cents (3.6%), with almost all of the loss coming in Friday COMEX trading. As a result of silver's pronounced relative weakness, the silver/gold price ratio widened out by two full points to 85.3 to 1. There was no big switching of silver to gold positions this week, as always; the price ratio changes big when silver moves big.

Over the last 14 trading days, silver had first moved higher by two and half dollars (15%) over the first 7 days and then moved lower by two dollars (10%) over the last seven trading days. One would think such large price moves for a world commodity would have to involve significant developments in actual supply and demand. However, I'm aware of no such developments that would account for the price volatility (and I try to follow these things fairly closely).

By process of elimination, the only possible cause for silver's sudden price volatility was trading in the COMEX silver futures, where daily trading volume exploded to the highest levels in years. The twist this time is that no real positioning changes were evident in the just-released Commitments of Traders (COT) report, quite contrary to my expectations (which I'll discuss in a bit). The unmistakable conclusion is that the extreme price volatility of the past two weeks (at least thru Tuesday) was purely the result of hyper speculative day trading on the COMEX, mostly by computer-generated algorithms.

Not for a moment am I changing my firm conviction that futures positioning on the COMEX is the main price driver and will determine prices in the future; but the data indicate it was frantic day trading that accounted for the price volatility of the past fortnight. When there's incredibly high trading volume, no big positioning changes and price volatility explodes, the only conclusion is that day trading is responsible for volatility. What's the big deal, one might ask?

The big deal is this – on its face this hyper day trading can only be the work of purely speculative traders (day trading never involves legitimate hedging). As such, the unmistakable conclusion is that excessive speculation, in the form of day trading, is responsible for the price blast up and then down in silver over the past two weeks. There is not a commodity law in existence that doesn't forbid excessive speculation to determine price – yet, in one form or another that is all that occurs in COMEX silver futures. And all the data pointing to excessive speculation comes from the very regulators (the CFTC and the CME Group) that should be cracking down on it.

There's a lot to cover, so let me run through the usual features quickly. The turnover or physical movement of metal either brought into or removed from the COMEX-approved silver warehouses surged this week to 7 million oz, the highest level in months. The movement was mostly of the "in" variety, as total inventories surged by 4.7 million oz to 316.2 million oz, a decisive new record high for COMEX inventories. Still no change in the JPMorgan COMEX warehouse – still stuck at 153.8 million oz for the 11th week.

While I had been hoping for a slowdown in turnover (I think), there's no way to predict future movements. I believe this week's movement and increase in inventories are related to continuing delivery demands for the September COMEX delivery month. As such, this is more bullish than bearish in that it suggests metal already in the warehouses is not sufficient enough to meet delivery demands

and new material must be brought in. Why go through the expense and logistics of moving new metal into position if you can more easily deliver metal already in place?

Total September silver deliveries are now up to 8197 contracts (41 million oz), by far the largest delivery month of the year and JPMorgan is still the largest stopper (taker) of silver deliveries at 1598 contracts (8 million oz) in its own house account. JPMorgan is also the largest stopper in gold this month in its house account, although this is not a traditional delivery month for gold.

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

While there was a large increase in total COMEX silver inventories this week, there was a larger outflow of roughly 10 million oz in the leading world silver ETFs. Before I get to that, a few words on the new short report on stocks.

Late Wednesday (well-after the mid-week article was posted), the new short report on stocks, as of the close August 30, was published and revealed that the short position in SLV, the big silver ETF, increased dramatically by 10 million shares to just over 21 million shares (ounces). (The short position in GLD dropped sharply). It was the largest two-week increase in years for SLV and, not coincidentally, was exactly as I hoped would be the case.

<https://quotes.wsj.com/etf/SLV>

To be sure, while I was certain that there was a big increase in the short selling of SLV shares into the rally that lasted through Aug 30, I was much less sure that a big increase would actually be reported. My doubts had nothing to do with whether there was a big increase in SLV short selling, but strictly with whether the increase would be accurately reported. My doubts lie in the legitimacy of the keeper of short sale statistics, the Depository Trust Clearing Corporation and the methodology of how the short statistics are compiled. I've discussed my concerns about the DTCC in the past and won't do so again today. However, the reported increase in the short sales in SLV does assuage some (not all) of my previous misgivings about the DTCC.

While I admit that this is somewhat esoteric and deep into the weeds, I believe this discussion should take place because it goes to the heart of some important matters in silver. The reason I was convinced that the short position in SLV increased sharply in the two week period through Aug 30 was because prices moved higher accompanied by heavy trading volumes and clearly reflected net investment buying, which, in turn, required substantial physical metal deposits. Yet, no big physical deposits were reported over this time. This was in stark contrast to the previous two-month period of high volume, increased prices and very large physical deposits into the SLV of nearly 100 million silver ounces.

On the previous period of large physical deposits into the SLV, the short position hardly budged and for good reason – the prompt physical deposits made short sales of shares of SLV unnecessary. On big net buying, it's one or the other – either timely big physical deposits or short sales of the shares. The all-important catch (as I pointed out previously) was that because it was obviously a single buyer on the previous purchases of SLV shares (upon conversion of COMEX futures contracts), that big buyer knew there had to be big physical deposits and would have screamed his head off to BlackRock (the owner of SLV) if those big physical silver deposits had not been made. In other words, the sellers knew they had to deposit metal.

The buying in SLV for the two weeks ended Aug 30 seemed much more to be many buyers and not a single big buyer as was the case previously. None of these many diverse buyers would have any inkling of how much silver was owed to the trust in total, so that cleared the way for the sellers to short the shares, since no one buyer could complain to BlackRock about insufficient metal being deposited. As a result of the big selling on Thursday and Friday of last week, I believe all the short sales added were bought back, eliminating the need to deposit metal and I would expect a big decline in the SLV short position in the next report.

The biggest takeaway from all this is that the physical silver market is tight, otherwise these games of only making deposits when necessary and avoiding them when not forced to do so wouldn't occur. And you can be sure that JPMorgan is more involved in these games than anyone else.

One additional point. There were notable withdrawals of physical silver from the SLV and other silver ETFs this week of more than 10 million oz. This could either reflect net investment selling as a result of the sharp selloff in price on Thursday and Friday of last week or something else. The something else could be the start of a conversion of shares to metal by the big silver whale who recently bought around 100 million ounces; first by buying 20,000 COMEX futures contracts and then by converting those contracts into shares of various silver ETFs. This is what accounted for the unprecedented physical deposits into SLV and other ETFs.

As I previously mentioned, it would not surprise me if the big silver buyer decided to further convert from ETF shares to metal held in the buyer's own name. One reason would be cost, as the ETFs charge a 0.5% annual management fee for storage and that could be negotiated to a cheaper storage arrangement. Saving 0.25% on the storage of 100 million oz would come to nearly \$4 million annually and wouldn't even necessarily involve physically moving the metal – just a few phone calls and some paperwork.

I don't know if the big buyer of 100 million oz of silver will move to further convert his ETF holdings into metal that he owns directly (if I were in his position, I know I would), but if he does it will show up as big withdrawals from the same ETFs that experienced the previous large deposits. I can't tell if this week's withdrawals of 10 million oz from a few big ETFs is the start of this process, but if the withdrawals continue and accelerate, it is likely that is what is occurring.

Turning to this week's COT report, the changes were far from what I expected. I couldn't have been more off in silver if I tried, as there was very little positioning change where I expected at least 25,000 contracts. There was the expected managed money selling and commercial buying in gold, but less than half of the 70,000 contracts predicted. Finally, JPMorgan didn't reduce either its silver or gold short positions. While no key moving averages were penetrated to the downside, gold did fall

more than \$50 in the reporting week, while silver fell more than a dollar.

In COMEX gold futures, the commercials reduced their total net short position by 32,100 contracts to 305,600 contracts. While it was the largest weekly decline in commercial short positions since April and the lowest position in 6 reporting weeks, it was nowhere near what I hoped for.

About the only constructive feature of this week's report is that over the past two weeks, roughly 25,000 commercial short contracts were closed out (in the swap dealer category). While prices were down substantially in the reporting week, the prices at which the short positions were originally established do indicate serious overall losses were booked and realized on the closeouts – roughly \$300 million or more. I can't attribute the realized losses to the 7 big shorts, so it looks at this point that they are hanging tough.

But realized commercial losses on short positions are almost unprecedented and there is no doubt that the commercial shorts seriously miscalculated how high gold (and silver) might climb when they started adding short positions aggressively in early June. By June 18, the commercials increased their total net short position by 115,000 contracts (11.5 million oz) at prices around \$1325 to \$1350. At the time, it looked to me that the commercials were hoping to rig prices lower than the 50 day moving average (then at \$1300), causing the managed money traders to sell long positions and for the commercials to clear about \$300 million net on a collective basis – a typical amount for a complete wash, rinse and repeat trade cycle, which the commercials would orchestrate two or three times a year.

Instead of a quick collective \$300 million profit in gold envisioned by the commercials in mid-June, the price of gold (and silver) rose and some commercials just booked a \$300 million loss by covering a fraction of the total short position. More importantly, the 7 big shorts which would only claim a good sized portion of the expected \$300 million collective profit had things turned out as expected, ended up being in the hole for nearly 20 times the expected total profit less than two weeks ago. These big commercial shorts may have turned things around at this point, but none need to be reminded that it isn't wise to risk billions in the hopes of making millions. Perhaps they will end up largely unscathed when the dust settles on the open positions that still must be resolved, but they just had a learning experience and fright that will not be soon forgotten.

As a result, if we do get a flush out to the downside, the odds on which have increased, the big (and smaller) shorts are not likely to venture so aggressively on the short side the next time prices start to move higher. I thought the commercials would see that without having to learn it the hard way, but sometimes the hard way is the only way.

The managed money traders sold 25,445 net gold contracts, comprised of the sale and liquidation of 25,700 long contracts and the buyback of 255 short contracts. I expected much more selling. While prices were down during the reporting week, it looks like the managed money long liquidation resulted in a realized profit of \$200 to \$300 million, coming close to the realized loss of the commercials who closed out shorts, given the zero sum nature of derivatives. The resultant managed money net long position of 206,181 contracts (239,475 longs versus 33,294 shorts) must still be considered bearish by historical conventional standards.

In COMEX silver futures, the commercials increased their total short position by a microscopic 100 contracts to 84,800 contracts, in the process establishing by the slimmest of margins the largest (most bearish) commercial short position in two and a half years. And here I was expecting a reduction of at

least 25,000 contracts. To make matters worse, JPMorgan appears to have increased its short position by 1000 contracts to 26,000 contracts.

On the managed money side, these traders were net sellers of nearly 1300 contracts, comprised of the sale and liquidation of 2728 long contracts as well as the buyback of 1432 short contracts. The resultant managed money net long position was 59,586 contracts (83,812 longs versus 24,226 shorts) is still bearish on an historical basis, although not as bearish as is gold's market structure, even after this reporting week.

As far as how I could be so far off, particularly in silver, I touched on it in Wednesday's missive, namely, that since no key moving averages were penetrated to the downside, perhaps the managed money traders didn't react to the sharp downdraft on Thursday and Friday of the reporting week. That would appear to be what occurred. I thought (overthought, obviously) that the managed money traders would be quick to nail down the largest open profits they've ever witnessed in gold and silver and would be quick to lock in some of those gains (they did a bit in gold). I also thought that these traders would be quick to add shorts, as they demonstrated recently when they added 10,000 new shorts in one reporting week.

Needless to say, neither event transpired which increases the odds that the managed money traders may get fully liquidated and put on new shorts on lower prices. (Although sudden news, like the drone attack on Saudi Arabian oil facilities can cause commercial price rigging plans to fall by the wayside). As far as JPMorgan not buying back any short positions in silver (or gold), it would appear that could only occur on big managed money selling which never materialized (in silver).

The basis for my final brick in the wall premise was that JPMorgan likely bought back most of its COMEX silver and gold short position, which clearly didn't occur. My reasoning was that had JPM bought back all its paper COMEX shorts (and maybe even get long) it was free to take its boot off the neck of prices to achieve maximum profit on its massive physical silver and gold holdings. While that's how I believed JPMorgan looked at things (taking care of itself to the exclusion of what's legal or not), not only would it be obvious to me should that occur, it might be obvious to others as well. Since JPMorgan is more capable of playing the game of skullduggery than even Prince Machiavelli himself, I also have thought that perhaps JPM might not be so obvious as to let silver and gold prices rip higher precisely at the moment of its greatest long exposure.

I guess what I'm saying and have said in the past, is that if JPMorgan is looking for some phony alibi or cover story for prices exploding and it not being blamed for holding some short position just might be that alibi as in, "don't look at us, we were short on the COMEX".

What brings this thought to mind (again) is the story circulating this week of two high-level JPMorgan precious metals employees being put on a leave of absence in connection with the Justice Department's ongoing investigation into spoofing and price manipulation on the COMEX. One of the employees was said to be the global head of base and precious metals trading for the bank, a senior position if ever there was. The other trader was involved in a spoofing case brought by the COMEX in 2017 for infractions occurring years earlier, in which no guilt was admitted or denied, but a \$95,000 fine was ordered, underscoring the repetitive nature of spoofing at JPM.

<https://www.cnbc.com/2019/09/13/jp-morgan-puts-traders-on-leave-amid-criminal-investigation.html>

Obviously, the news of the senior employees being placed on leave is not the result of a public release by JPMorgan in the interest of full disclosure, but rather from an unofficial source. Come to think of it, even getting JPMorgan to acknowledge that it is engaged in precious metals, to say nothing of it having an ironclad control on price, is not something I've ever seen. My experience is that you can call JPMorgan a stone-cold precious metals crook, explain why and send it to its CEO and Board of Directors and they will all look the other way. Used to be if a bank was openly called crooked, that bank would react, but lots of things used to be.

However, the leaking of the news that two senior employees have been suspended does bring us back to the Justice Department's ongoing investigation and the two criminal guilty pleas entered by more junior JPM traders. Those guilty pleas specifically referred to more senior traders having knowledge and supervision over the junior traders, so it would appear the DOJ is just lining up all the JPM ducks in a row.

In this perspective, the Justice Department has already been wildly successful by securing guilty pleas for spoofing with the distinct probability of continued prosecutorial success along spoofing lines. What's made the DOJ's efforts to date so successful is that spoofing is an incredibly specific illegal act - easy to prove. All that needs to be proven is that large orders were entered and immediately cancelled and that caused prices to move so that a different sitting order could be executed. This does require time to study the detailed trading records, but this data does exist and, therefore, a firm paper trail exists for the DOJ to follow.

The irony, of course, is that spoofing was overlooked by the regulators for years, even though it was always completely devoid of any economic legitimacy. But the trading records are required to be kept and this has resulted in the regulators, now including the DOJ, to go back and prosecute spoofing from years ago. Quite literally, the Justice Department going after spoofing cases is the closest a prosecutor can come to shooting fish in a barrel.

The good news is that better late than never and because spoofing is now recognized as being clearly illegal, it's hard for those who have been uncovered to have participated in spoofing to mount an effective defense. That's why, for instance, Merrill Lynch/BankAmerica completely folded with no fight, agreeing to a deferred prosecution settlement for what amounted to a limited amount of spoofing by a couple of rogue traders. By comparison, JPMorgan is the mother ship of spoofing, as the guilty pleas to date reveal.

The bad news, of course, is that spoofing is but a very small tip of the illegal precious metals iceberg run by JPMorgan. It's like prosecuting a serial killer for a traffic infraction. JPMorgan should be prosecuted for far more serious precious metals manipulation issues and antitrust behavior than just spoofing, even though these other issues are many times more difficult to prosecute. That leaves me with the question of is the Justice Department aware of just how much JPMorgan manipulates and controls precious metals prices or does it just see spoofing?

The answer is important because if the DOJ is using spoofing as a lever against the wider JPMorgan manipulation, then nothing could be better. But if it sees only spoofing and little else, then nothing could be worse. Until the late Bart Chilton's interview, I had questions about whether the CFTC had any idea what JPMorgan was up to, but not afterward. The problem was that JPMorgan was too formidable of a legal adversary to confront.

I've also thought that the Justice Department might not be up to taking on JPMorgan, but the good thing is that spoofing allows the DOJ to go after JPM on incredibly simple grounds that can be used to apply pressure on other more serious illegal acts. We should soon know which it will be based upon JPMorgan's behavior ahead.

As far as where this week's positioning leaves us, barring outside surprises, the odds have increased that we may see a flush out to the downside, since there has been so little managed money selling to date. What it means for me is to stretch out the time period for which I plan to buy additional options to allow for lower prices, without abandoning any core silver positions. If JPMorgan and the other big commercial crooks succeed in rigging prices lower yet again, I'd like to time my last purchase to when the rig is done.

I should mention that while I saw some potential changes in COT positioning (perhaps by looking too hard) that never materialized, I was taken aback by the many commentaries citing the negative market structure as the reason to be cautious on prices. While I would have much preferred being close to accurate this week, I am encouraged that so many have adopted COT positioning in their analysis and for good reason.

As far as the running financial tally for the 7 big commercial shorts in COMEX gold and silver, this week's \$20 drop in gold and 65 cent drop in silver brought \$700 million in relief to the big shorts, reducing their net collective open loss to \$3.4 billion as of yesterday's close. An asterisk of sorts needs to be added to account for the highly unusual \$300 million realized loss booked by other smaller commercials and perhaps including some of the big 7.

Ted Butler

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Silver – \$17.53 (200 day ma – \$15.59, 50 day ma – \$16.93)

Gold – \$1495 (200 day ma – \$1346, 50 day ma – \$1478)

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