August 3, 2013 – Weekly Review

Weekly Review

During a week with the customary price volatility on Friday said to be due to the monthly employment report, the price of gold ended $20 (1.5%) lower, while silver fell 10 cents (0.5%). I know the employment report always influences gold and silver prices, but I've given up in trying to understand why. As a result of silver's relative outperformance to gold this week, the silver/gold price ratio tightened in slightly to just over 66 to 1, but this level is close to the most undervalued silver has been relative to gold in three years. Make no mistake, I think gold is on the verge of a significant move up, but I would switch from gold to silver in a heartbeat based upon all the facts as I know them. That's because, in the end, silver should exceed whatever gains gold achieves by a wide margin.

For the second consecutive week, turnover within the COMEX-approved silver warehouses was extremely active, as more than 4 million oz moved into and out from the warehouses. Total COMEX silver stocks climbed by 1.2 million oz to just over 164.5 million oz. To my mind, the persistent and elevated silver metal turnover over the past two and a half years still signifies tight conditions in the wholesale physical silver market.

There is another aspect to COMEX silver stocks that has become noticeable the past few weeks. There have been a number of obvious transfers of trailer-sized shipments of silver (600,000 oz) from various COMEX warehouses into the warehouse run by JPMorgan. The most plausible explanation is that the silver shipments into the JPMorgan facility come as a result of the bank taking delivery of over 14 million oz in their own name during the just completed COMEX July contract delivery period. The silver shipments into the JPM warehouse make sense as why would the bank pay someone else for storage when JPMorgan has its own warehouse? On that basis, it would not be surprising to see additional shipments into the JPM facility.

There was some relatively small decline in the metal holdings in the big silver ETF, SLV, of around 700,000 oz this week, following deposits of over 13 million oz over the previous weeks. By contrast, the standout feature continues to be the persistent withdrawals in the big gold ETF, GLD. From year end, silver deposits in SLV are up 12 million oz (3.7%), while gold withdrawals in GLD now total 13.9 million oz (32%). Since I believe the liquidated gold from GLD is now in strong hands (primarily JPMorgan's), I don't view the gold liquidation as negative to the price from here; although it certainly was while it occurred. I further believe that JPMorgan got hold of tens of millions of silver ounces from SLV over the past eight months, despite there being no net decline in SLV holdings. The salient theme here is not the contrast in that the holdings in SLV were steady or grew while GLD fell; the common denominator is that JPMorgan rigged the price of each lower to buy whatever of each it could. More on that in a moment.

Sales of American Silver Eagles ended as reported in Wednesday's article, at just over 4.4 million coins for August. This was the strongest month since January, although it did get a boost from some sales being held over from July. The US Mint seems to have increased its production capacity to around 4 million one-ounce Silver Eagles per month and is still rationing Silver Eagles by allocation. By contrast, sales of American Gold Eagles recorded their lowest monthly sales of the year in August, pushing the silver to gold sales ratio to the highest in memory, at over 87 Silver Eagles to every Gold Eagle.
http://www.usmint.gov/about_the_mint/index.cfm?action=PreciousMetals&type=bullion

You may have assumed that I would use this contrasting data to emphasize how much stronger relative demand was for Silver Eagles than for Gold Eagles, but I have something else in mind. As I have alluded to recently, I don't know where demand for Silver Eagles is coming from. It does not appear to be from plain vanilla retail demand according to anecdotal reports from domestic retail dealers or from COT data which indicate near record low public participation on the long side (the non-reportable category). In the past, when the American retail public bought Silver (or Gold) Eagles aggressively, there was no doubt they were buying. Today, we have no indications of aggressive retail buying, yet the US Mint is pedal to the metal in selling Silver Eagles, with sales for 2013 way ahead of any previous year to this point. The obvious question is who the heck is buying all these Silver Eagles?

By process of elimination, if it is not domestic retail demand, it has to be either foreign demand by buyers in broad numbers or a single big buyer, domestic or foreign. I mentioned the possibility on Wednesday that it might be JPMorgan and the more I think about it, the more that makes sense. I certainly don't think that JPMorgan has been the exclusive buyer of Silver Eagles, but the bank has been so aggressive in buying silver and gold in various forms over the course of this year's historic price decline, that there is little reason to think they wouldn't be buying Silver Eagles as well. After all, if the bank could purchase one to two million Silver Eagle coins per month, in a relatively short time quantities approaching JPMorgan's 14 million oz taking of July COMEX deliveries could be achieved.

An alternative question might be why isn't JPM buying aggressively in Gold Eagles as well, but the bank has been able to buy such massive quantities of gold elsewhere (GLD and on the COMEX) that it hasn't had to resort to buying gold from the US Mint. It is my opinion that because silver is so much tougher to buy in dollar quantity than gold, JPMorgan would leave no stone unturned in its intense quest to buy as much silver as possible, including buying Silver Eagles. If I am correct, that's not negative for gold, but is super positive for silver because it highlights just how badly JPM wants silver.

The changes in this week's Commitments of Traders Report (COT) were largely as one would expect for a reporting week which featured lower prices almost every day for silver and gold. Then again, considering how much speculative selling/commercial buying has already occurred this year on the epic price rig to the downside, it would be unreasonable to assume there is much more to go.

In gold, the headline number of the total commercial net short position declined by 8900 contracts, to 25,800 contracts. It's difficult not to repeat oneself in describing just how extremely low (and bullish) is this commercial net short position in COMEX gold, so please don't let its extremity get dulled by the market remaining near current readings for the past month or so. By commercial category, the big 4 shorts bought back over 6000 short contracts and the raptors bought 4000 new longs. The big 5 thru 8 shorts sold the balance of a thousand or so contracts in new short sales.

In silver, there wasn't much to report, except that the total commercial net short position declined by 1800 contracts to an unbelievable (to me) total short position of 8300 contracts. Having studied the COTs for 30 years, I find it hard to believe we could be this low in the commercial net short position without a price explosion. Yet. This week the 4 big shorts did most of the heavy lifting by buying 1400 short contracts back, while the raptors maintained a net long position of 41,200 contracts. As in gold, the silver market structure has been locked and loaded to the upside, but has been in that position for many weeks.

The most significant aspect to the gold COT report was that it confirmed that the data in the previous report was correct in that there was an increase of nearly 10,000 contracts in the net long position of the four biggest longs, to over 140,000 contracts. While that record net concentrated long position (by the big 4 longs) didn't increase this week, neither did it decrease. This week's COT report indicates that the concentrated long position in COMEX gold is the largest it has ever been compared to the concentrated short position. I never thought I would see this happen. This increases my confidence that JPMorgan is holding a record net long position in COMEX gold futures of 85,000 contracts (8.5 million oz).

I know that it may seem that I have been making a big deal out of JPMorgan's newly acquired massive net long position in COMEX gold, but in truth, there is nothing more important. Let me rephrase that Â? nothing even comes close to being as important than the concentrated long position that JPMorgan holds in COMEX gold futures. Others can persist in trying to divine the undocumented statistics and pronouncements from the LBMA, or in what central banks may or may not be doing; I wish them well. For me, I'm sticking to the hard data that can be verified.

What that hard data tell me is that JPMorgan has, effectively, cornered the gold market. Think I'm exaggerating? This week's COT report indicates that the 4 biggest longs hold 140,550 contracts. That is a very hard number derived by multiplying total COMEX gold open interest of 397,035 contracts by the percent of 35.4% held by the 4 largest traders on a net basis from either the futures only disaggregated or legacy long form reports. (The CFTC doesn't give you the concentrated figures in contract terms; you must do some minor calculations to get them). Of the 140,550 contracts held net long by the 4 largest traders, I am calculating that JPMorgan holds 85,000 contracts based upon previous COT and Bank Participation Report data. Please stick with me a minute while I go over some basic numbers. It's either this way or resorting to made up stories.

By subtracting the total number of spread contracts listed in the disaggregated COT report of 60,802 contracts from the total open interest of 397,035 on the cut-off date, there remains a true net total open interest of 336,233 contracts in COMEX gold futures. Dividing those 336,233 contracts into the 85,000 contracts that JPMorgan holds, the resultant percentage is 25.3%. In simple terms, JPMorgan holds more than 25% of the entire COMEX gold futures market on a true net basis. There has never been a more concentrated net long position in any major regulated futures market in history. Not even the Hunt Brothers in COMEX silver in 1980 or the Sumitomo copper trader, both found to have manipulated markets by means of a corner, held as much a share of the market as JPMorgan holds now in COMEX gold futures. Here's very recent account of the Sumitomo copper manipulation, by a trader named Â?Mr. 5%"
http://au.finance.yahoo.com/news/copper-king-empire-built-manipulation-154800854.html
Keep in mind, that JPMorgan's concentration in COMEX gold futures is five times the copper manipulation level. If a 25% net share of a market does not represent a corner, then that term has no meaning. I'm not alleging that JPMorgan owns 25% of all the gold in the world, as that would be impossible. Heretofore, I would have insisted that owning 25% of the COMEX gold market was impossible, but no longer. And there's more.

As I mentioned on Wednesday in the London Phony Baloney article, any move to backwardation purported to exist on the LBMA, must find its way to the COMEX (since the COMEX was the only market with verifiable data and regulation). In the past few days, since the start of the August delivery period for COMEX gold contract, there are signs of backwardation.

First, a word on backwardation. The term as is generally intended indicates such tightness and a shortage of immediate deliverable supplies of a commodity that buyers (mostly industrial users) are willing to pay a premium for the immediate delivery of the commodity rather than wait for cheaper supplies later. Generally, periodic shortages can and have occurred in any commodity that is consumed to the point of there not being sufficient supplies on a prompt basis. Grains, energy products and industrial metals are prone to backwardation when supplies get tight.

I fully expect this backwardation and premium pricing condition to come to silver as and when the industrial users panic at signs silver deliveries will be delayed due to a shortage of immediate supply. I've always been skeptical of a gold shortage for the simple reason that gold is the one commodity that is not consumed industrially and, therefore, can't go into a shortage. That's not to say gold can't go up in price for many other reasons; but with additional gold supply being added every day to world inventories and little industrial consumption to reduce the amount of gold, the concept of a gold shortage seems counterintuitive.

But there is no denying that the price of the current COMEX August delivery month is slightly higher than the delivery months of October and December and that technically meets the definition of backwardation. The only question is what is causing the backwardation, slight as it may be to this point. Is it caused by the stories emanating out of London, suggesting massive and insatiable demand, mainly from Asia, met with central banks leasing and dumping metal in a panic to keep the lid on the gold price? Or is it something else? We all have to decide for ourselves.

Based upon the public data, there would appear to be little net investment buying of gold (or silver) over the course of this year from the West (US and Europe). Instead we have witnessed record net investment selling, in both ETFs and COMEX futures. After a spurt of buying in Gold Eagle on some big price takedowns, that demand has dissipated, at least temporarily. I don't deny there has been buying from India and China, although the quantities are difficult to pinpoint. I do think JPMorgan has been buying massive quantities of gold and silver, but that's different from insatiable demand from Asia that the central banks are struggling to meet.

Instead, I believe that JPMorgan has purchased its massive quantities of gold and silver by rigging prices lower to induce selling from speculators and investors in GLD and on the COMEX, as I have been writing about all along. Now, even the backwardation in COMEX gold futures can be laid at the feet of the bank's corner on the gold market.

For the first few days of deliveries on the August contract, of the 1962 total contracts delivered, JPMorgan has taken 1206 contracts (61%) of those deliveries in its house or proprietary trading account. Additionally, customers of JPMorgan have taken (stopped) another 260 contracts, raising to 75% the share of deliveries taken by JPMorgan -affiliated accounts on the COMEX August contract. With close to 3000 August contracts yet to be closed out or delivered upon, clearly JPMorgan holds in its power the fate of the backwardation issue in COMEX gold. Not only does this add to the confirmation that JPMorgan is massively long in COMEX gold futures, it represents a decided change of behavior on the bank's part from formerly being the big issuer of gold deliveries when it was massively short earlier in the year. Here's some data that might seem confusing at first, but that provides the documentation for what I am alleging, namely, that JPMorgan has the death grip of a corner on the long side on COMEX gold.
http://www.cmegroup.com/delivery_reports/MetalsIssuesAndStopsYTDReport.pdf

Last December 1, JPMorgan was net short around 75,000 contracts of COMEX gold futures. The bank has since flipped that position, on the price smash orchestrated by the bank, into a long position of 85,000 contracts. That means JPMorgan flipped a 7.5 million oz gold short position into an 8.5 million oz long position on the COMEX alone. Throw in additional gold positions that may easily total an additional 12 million ounces (from GLD and yes, even from the LBMA); I estimate JPMorgan's long position in gold to total at least 20 million ounces, or the equivalent of more than $25 billion.

On a $300 up move in gold, JPMorgan would stand to make $6 billion and $2 billion for every $100 on top of that. I would remind you that these sums might seem outlandish for most entities, but for JPMorgan these are not out of scale. After all, this is a bank that makes $25 billion a year in net profits (even after paying out billions in regulatory fines and settlements). With profits under pressure from encroaching and long overdue regulations, a timely gold score would come in handy for the bank, although I still believe it is in silver that the bank is most exposed to on a regulatory liability basis and the one they are most eager to wash their hands of.

While I can analyze what positions JPMorgan holds based upon the documented data, I can't know its intentions. That is where you come in. I can tell you what the set up looks like and what I think will occur because of it, but I'm not a prophet or guarantor. It looks to me that JPMorgan has amassed such a massive long position in gold and such a massively reduced short position in silver that expecting a price explosion seems most reasonable. Maybe by pointing it out, it may cause JPMorgan to alter its plans, but what's my alternative Â? skip reporting on the facts and instead make up undocumented stories about massive buying in places that can't be verified?

A couple of months ago, I wrote about the certain coming resolution of gold and silver prices finally penetrating the important moving averages to the upside. When this penetration occurred, it would trigger technical and momentum type buying in the same manner that it triggered technical selling to the downside. That process has been delayed as JPMorgan continued to press prices in order to buy more gold and silver positions, but the resolution is still certain and closer than ever. In fact, gold has been dancing on its 50 day moving average for the past two weeks and silver is within less than a dollar from its 50 day moving average (at $20.56). Sooner or later, the moving averages will be penetrated and we will gain knowledge of what JPMorgan intends to do with its corner on the long side of the gold market and its successful liquidation of its silver short position.

Also a little while back, I commented that JPMorgan holds the key to everything. That goes for price direction and intensity and now to the backwardation issue. If JPMorgan wants prices to explode, prices will explode. If JPMorgan wants severe backwardation, that will occur. We can only guess what they may do, but my bet is on them doing what's best for them. Based upon the record of what positions the bank has taken, it's hard to imagine JPMorgan not forcing prices sharply higher at some point.

Ted Butler

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Silver – $19.90

Gold – $1313

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