

December 6, 2017 - Probabilities Win Out (Again)

Regardless of what happens pricewise from here, it's safe to say that the higher probability of some type of flush out to the downside in gold and silver has occurred. Perhaps it is too soon to proclaim that the flush out is complete, but I'll get to that in a moment. At this point, it's important to establish that yesterday's downward penetration in gold of its 200 day moving average, for the first time in five months, was the "official" confirmation that the probabilities won out again.

Of course, the greatest probability since the price highs of early September (\$1350 in gold, \$18.25 in silver) was that the commercials would eventually induce enough managed money selling at low enough prices to signal yet another trading victory over the technical funds. Yesterday's penetration in gold was the last remaining barrier in declaring the commercials as the victors for this go-around. It also explains why gold and silver prices have fallen for the past three months, namely, so that the commercials could buy as many gold and silver contracts as the managed money traders could be induced into selling.

Yesterday, the commercials engineered the gold price down to what has always been low enough to trip off robust managed money selling, which I'm confident will be reflected in Friday's new COT report. Silver, having been mostly below its two key moving averages (the 50 day and 200 day) for much of the past couple of months, has continued to set new price lows. As such, the resolution of the market structure in silver is much more advanced than it is in gold.

The billion dollar question is if silver's market structure has advanced enough to signify a bottom. In many ways I believe the answer may be yes and in two other ways maybe not. I'm still concerned that there may be more selling in gold from the managed money traders and should that occur, lower gold prices tend to coincide

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with lower silver prices. My main concern is still if the managed money traders will add aggressively to short positions. I would imagine the managed money traders may have added to silver short positions already and that will be reflected in Friday's COT report (along with managed money long liquidation), but I'm still asking myself if they will add tens of thousands of new short contracts starting from today onward. Unfortunately, I still don't have the answer as it is unknowable in advance. Ask me after the fact and I promise I'll know then. At this point, it's guesswork.

Having been as nervous as a long-tailed cat in a room full of rocking chairs for the past three months, worried that silver would rocket higher with me not fully aboard, I have now replaced virtually all of the chips that I took off the table in mid-Sep. I've already spent about a third of the dollar amount saved by doing so on irresponsible short dated out of the money call options and fully intend to spend the rest on similarly irresponsible additional calls on lower prices and the passage of time. Again, this is not intended as an invitation for anyone else to do likewise, I just had to buy enough silver to get back to my sleeping point. I would still avoid margin like the plague.

Long time readers should know that I am always too early in fleshing out market structure bottoms, but I just don't seem able to avoid that given what I think is the real story in silver. In my defense, I believe silver prices always worked higher eventually from all previous market structure bottoms; but because buying at such times involves catching a falling knife, short term results can be painful, at least temporarily. Forewarned is forearmed and all that jazz.

It appears to me that much of the remaining managed money technical fund long position in silver may have been liquidated in the downdraft through yesterday's

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cutoff for the reporting week. The last COT report indicated the potential for perhaps an additional 14,000 long contracts to be sold should the previous core long position of 56,000 contracts hold. It's always possible that the core non-technical fund long position could expand or contract. In other words, we might be at or close to the core long position now. That elevates and sharpens the question of whether the managed money traders will add big amounts of new shorts. I would remind you that the lower silver prices go, the stop loss close out point for new technical fund shorts grows larger. Today, we are more than a full dollar below silver's 200 day moving average, making the risk/reward equation much less attractive for new short positions.

If there are tens of thousands or close to that amount of new managed money short contracts to be established, then we're going lower in price. In that case, we would end up with a much better market structure than otherwise, although not without the pain of lower prices. If not, silver prices shouldn't go or remain lower for long. This has been the main market structure condition all along. But what's truly got my attention now is the continued drama, as I see it anyway, in the COMEX gold and silver December deliveries. Normally, I discuss deliveries in the weekly review, if there is anything special to comment on. For months, I have hardly mentioned COMEX deliveries, mainly due to the absence of activity by JPMorgan in its house account. That all changed with the December deliveries, which commenced a week ago.

Through today, the December deliveries have taken center stage in both gold and silver. Remarkably, I have seen much commentary on EFP's - Exchange for Physical transactions, a delivery feature which leaves many unanswered questions; but hardly any commentary on the extraordinary hard data available on straight, plain vanilla COMEX deliveries.

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Let me point out why deliveries are important in the first place. If one contends that silver and gold prices are manipulated by paper contract positioning on the COMEX, as I certainly do, then one is asserting that paper positioning dictates price to the physical market. A key feature at the heart of why paper positioning controls physical prices is the mechanism by which paper contracts can be converted into physical. That mechanism is the delivery process and its existence is what legitimizes the COMEX. The vast majority of the time, those buying or holding long paper contracts choose to roll over their positions, rather than accept physical delivery, which entails the full payment of the contract's value and not just a small percentage in the form of margin requirements.

If there were no physical delivery mechanism in COMEX metal futures contracts, it would not be possible that the contracts would be as widely held and traded as they are. But not only does the physical delivery mechanism legitimize COMEX futures contracts, it also threatens to undermine the paper manipulation. The COMEX delivery mechanism makes it possible for physical to trump paper. All that needs to occur for physical to trump paper is for enough paper contract buyers to demand more physical metal than the sellers can provide, something on which we would all agree. The best way of determining that is to review the delivery data with an eye towards any unusual mismatches or unusual features. The current December COMEX deliveries seem to qualify in the unusual department.

In COMEX gold futures, there have been a large number of total contracts issued (5995), but an unusual feature is that one bank, HSBC has issued 4465 contracts in its own house account or nearly 75% of total gold deliveries. (Nearly 3000 contracts were issued by HSBC just today). It should be pointed out that HSBC had taken (stopped) around 6000 gold contracts in COMEX deliveries over the past year. Even

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more unusual is the emergence and reemergence on the stopper side of COMEX gold deliveries this month.

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

JPMorgan has been the biggest gold stopper or taker with 3602 contracts stopped through today in its house account. JPM had issued 1600 gold contracts in October and those contracts appeared to have been acquired earlier in the year. JPMorgan had previously been a big gold stopper in prior years and I consider the bank's return to be instructive. Even more striking to me is the emergence of Goldman Sachs as the second biggest gold stopper this month, also in its house account. So far this month, Goldman has accepted delivery of 1672 gold contracts and together with JPM, the two mega banks have taken 5274 contracts or 88% of the total gold contracts delivered.

Let me summarize. To this point, one bank acting on its own behalf (and not for clients) has issued nearly 75% of total gold deliveries, while two other banks, JPMorgan and Goldman Sachs, also acting for their own benefit and risk have taken 88% of all COMEX gold deliveries. That's pretty big doings to me. The COMEX delivery data this month is akin to the signs left in the jungle after a few big elephants have fought it out during mating season. These are the premier financial firms dealing in precious metals and it is hard to conclude that there isn't some type of dust up of unprecedented proportions occurring in the one feature that we would all agree is related to a possible trumping of physical over paper. That's the whole purpose of studying delivery data in the first place. If this data doesn't send your thoughts into overdrive, what data would?

In COMEX silver deliveries, it also appears to be a case of HSBC aligned against

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JPMorgan and Goldman Sachs. In a twist, Goldman actually redelivered 110 of the 1683 silver contracts it stopped previously, leaving them as having taken 1573 net contracts to date. That's still above what has always been the supposed COMEX limit of 1500 silver contracts allowed in any one month and my hunch is that Goldman may have been "persuaded" to reduce its delivery take down to that level. That's strictly speculation on my part.

What's not speculation is that JPMorgan is now up to 2323 silver contracts stopped and appears in position to stop as many as 500 contracts more, based upon remaining open interest. Clearly, no one persuades JPMorgan to do anything it doesn't want to do. Together, Goldman Sachs and JPMorgan have stopped a net of 3896 contracts of the 5147 total silver contracts issued this month, or more than 75% of the total. HSBC, in both its house and customer(s) accounts, has issued 3266 silver contracts or more than 63% of all silver contracts issued. While the percentages in gold appear to be a bit more telling at first blush, the real world equivalent numbers in silver are much more compelling to me.

If the delivery data in gold and silver are any indication of physical beginning to overpower paper, then there could be no more profound reason to expect prices to quickly bottom out and then surge. That's why I'm rushing things a bit in replacing silver positions previously sold and upping the ante for a big move higher via kamikaze-type call options. I'm not terribly surprised that the commercials have succeeded to date in rigging prices lower and generating managed money selling, as that was the high probability bet all along. I believe I have conveyed that all along.

What does surprise me is the delivery data to date. If you told me a week ago that JPMorgan would return to stopping prodigious quantities of physical silver and gold,

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I might not have believed you (although I would be hoping you were correct). But if you told me that Goldman Sachs would suddenly be taking large quantities of physical silver and gold in its own name, I would have not only disbelieved you; but also have admitted that the thought would have never crossed my mind.

Yet, here we are, one week later and staring down the gun barrel of both JPM and Goldman taking giant quantities of both silver and gold. Please add this to the long list of things I couldn't make up if I tried. How could I not be now pulling the trigger, perhaps prematurely, in repositioning previously sold silver positions and getting sucked into call options that don't appear to have a chance of becoming profitable?

As far as what to expect in this week's new COT report, I would look for big managed money selling (both long liquidation and new short selling) as well as big counterparty commercial buying (both new longs by the raptors and short covering by the big 8). I'd throw out ball park numbers of 30,000 net contracts in gold and 15,000 contracts in silver and, hopefully, more.

While I fully admit that prices could get rigged lower still, it is time to begin focusing on the next up move. I also admit that the big move up has yet to occur, despite my thinking that we have been at the doorstep of such a move on countless past occasions. The next move up could (and should) be the big one. The delivery data this month points to this being the last roundup.

Ted Butler

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Silver - \$16 (200 day ma - \$17.11, 50 day ma - \$16.92)

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Gold - \$1267 (200 day ma - \$1268, 50 day ma - \$1283)