February 27, 2019 – Caught in a Trap

Iâ??ll get into the latest data from yesterdayâ??s Commitments of Traders (COT) report as of Feb 12, but I am more looking forward to this Fridayâ??s report because it will include at least one day of the recent surge in gold and silver prices. Instead of jumping right into the actual numbers, I thought it might be more instructive to first step back and try to put things in a wider perspective.

It occurs to me that all of us are caught in a trap when it comes to gold and, most particularly, to silver. I would define â??all of usâ?• as including me, you (and all precious metals investors), all gold and silver producers and consumers, and certainly everyone involved in direct trading of COMEX futures contracts, including all the banks (JPMorgan especially), the managed money traders and the regulators at the CFTC and the CME Group.

My point here is that even though the banks and managed money traders have created, under the approval of the regulators, the price control and manipulation from which no one in the world of precious metals is exempt, all are necessarily and nonetheless caught in the same trap. Also included in the trap are all those who recognize or, ironically, fervently deny that gold and silver prices are manipulated. Thatâ??s the basic premise of price manipulation and why it is the most serious market crime of all, namely, because it traps everyone alike, even those causing or denying the manipulation.

Without drilling down to the actual numbers, the manipulation has been created and maintained by extraordinarily large numbers of COMEX futures contracts being traded between very limited numbers of market participants, most of which have no connection to the actual production, consumption or merchandizing of metals. Let me correct that a bit â?? itâ??s not so much that the numbers of COMEX silver or gold futures contracts being positioned are out of line with the futures trading of other commodities; itâ??s much more that the quantities of metal represented by the futures contracts are so out of line, particularly in silver, with the quantities in any other commodity so as to seem inconceivable. For instance, no commodity, away from COMEX silver futures, has a total open interest that is greater than the real world production of that commodity.

I suppose simply having a total long and short position (total open interest) greater than annual world production or consumption may not be enough to trigger regulatory inquiry (although it certainly should be enough), but what puts COMEX silver futures over the edge is the incredible concentration of the open interest, particularly on the short side. Concentration is the term (chosen by the CFTC) to describe the number of contracts held by a small number of traders. By tradition, the number of traders for which the CFTC has chosen to report the concentration data are the 4 and 8 largest traders in every commodity.

Itâ??s important to understand that the reason the CFTC closely monitors and reports on concentration data in every commodity is because concentration is the number one requirement for there being a manipulation, which, not coincidently, happens to be the CFTCâ??s main mission to guard against. In other words, the CFTC knows that the easiest way to prevent a manipulation is to prevent an unnecessarily large concentration or too large of a position being held by a small number of traders.

Current COT concentration data have indicated that the concentrated net short position of the 8 largest traders in COMEX silver futures is over 100,000 contracts or the equivalent of more than 500 million ounces â?? more than 60% of annual world mine production. No other commodity has or has ever had such an extreme concentrated short position. Moreover, itâ??s also easy to see that the price of silver is so low (because the concentrated short position is so large) and that none of the concentrated short position represents legitimate hedging and instead, is due to rank speculation by banks.

So how does the CFTC avoid dealing with the facts it is reporting? By being cute and intentionally misleading. It does this by deliberately avoiding making the obvious conversion of the number of contracts into what those contracts represent in actual world amounts. Reporting that the eight big traders hold 100,000 contracts short is a lot more antiseptic and clinical than concluding that is also 500 million ounces and 60% of annual world mine production and that none of these traders are legitimately hedging; and that no other commodity comes close to such equivalent numbers as reported in COMEX silver futures. The CFTC keeps pretending that no conversion is necessary.

It pains me to say that this deception by the CFTC has worked for more than 30 years â?? go count the number of commentators who point towards the unprecedented concentration in COMEX silver futures. You will find hardly any. Thatâ??s not to say there hasnâ??t been an explosion in commentary about the COT reports and price manipulation; just hardly any discussion about the concentration. If I had to pick the one single factor that has enabled the silver manipulation to exist for as long as it has existed (30+ years), it would be the failure to recognize the true nature of the concentration on the short side of COMEX silver.

This is another way of saying that the collective failure to put the concentrated short position in COMEX silver futures into proper perspective is the single biggest reason everyone is caught in a trap of which there is no easy way out. Presently, the concentrated silver short position is so extremely large that its resolution guarantees either a sharp drop in price in which the managed money traders will sell aggressively (as always) or an even sharper price rally in which, for the very first time, the big concentrated short sellers are forced to buy back short contracts at great loss. No one can escape the eventual resolution regardless of how long it may take. Thatâ??s the problem with the trap of manipulation â?? no one can escape its effects.

While we have all been in this particular circumstance on numerous past occasions, there is a new entity that is, for the very first time, now also caught in the trap â?? the US Department of Justice. By virtue of its public announcement on Nov 6, in which it openly confirmed an ongoing investigation into precious metals trading on the COMEX, the Justice Department has joined the ranks of those caught in the trap of the silver manipulation. I openly admit to being quite encouraged and absolutely thrilled by this development, due to my high personal opinion of the Justice Department, but I also freely acknowledge that my high hopes could very well turn out to be dashed if the DOJ fails to follow through as I envision it will.

Therefore, while the Department of Justice is now fully involved in an ongoing investigation of COMEX precious metals, there can be no absolute assurance it will see the concentrated short position in COMEX silver futures as Iâ??ve described it. Itâ??s also quite true that I have been optimistic in the past about the silver manipulation being brought to an end by regulatory insistence, only to be disappointed in the end. Specifically, I sang the praises of former CFTC chairman Gary Gensler nonstop for his pursuit of legitimate speculative position limits, only to see those pursuits falter in the end. In hindsight, I attribute Genslerâ??s failure (and mine) to the weak standing of the CFTC in overall federal agency importance.

However, there is a vast difference between the relative standing among US federal agencies between the CFTC and the US Department of Justice. The CFTC was, clearly, at the beck and call of the US Treasury Dept. and the Federal Reserve as became evident in the takeover of Bear Stearns by JPMorgan in 2008 and the subsequent lying by the CFTC months later in publicly denying that any problem existed on the short side of COMEX silver (Bear was the biggest COMEX silver short when it failed).

The Justice Department, from everything Iâ??ve observed over my lifetime, is no pushover, as was and is the CFTC. Thatâ??s not to say Iâ??ve always agreed with everything the Justice Department has pursued or that it has not failed in many of its pursuits, but the DOJ is no lightweight or pushover in terms of federal agency rankings. I may be mistaken, but no other federal agency tells the Justice Department what to do or not to do. The three divisions that are on the record as conducting the ongoing investigation into COMEX precious metals trading, namely, the Criminal Division, the FBI and the US Attorneys Division, are not known for taking orders from other federal agencies. In addition, Iâ??m hopeful that a fourth division, the Antitrust Division, takes up the issue of the price-fixing control of the concentrated short position.

Iâ??m hopeful that the Justice Department will take note that no one, not the CFTC, the CME, JPMorgan, nor anyone else will openly debate (or even admit to) the merits or lack thereof on the matter of the concentrated short position in COMEX silver futures. Itâ??s hard for me imagine that this is lost on the premier investigative and law enforcement authority in the US, but time will tell.

As far as yesterdayâ??s release of the (still delayed) COT report, the reporting week covered positions as of Feb 12, in which prices of both silver and gold traded mostly flat to slightly lower. As such, it was not expected that there would be managed money buying and commercial selling and there wasnâ??t much of either, but with a twist.

In COMEX gold futures, the commercials reduced their total net short position by 5100 contracts to 126,100 contracts. I am still struck by how small (and bullish) the total commercial net short position is following a three month and $130 rally in gold prices. Since the overall positioning changes werenâ??t large, I wonâ??t describe them in detail.

However, it is important to note that despite the overall reduction in the total commercial net short position, the concentrated net short position of the 8 largest traders (all commercial banks) rose by 2300 contracts to 199,955 contracts, the highest since last summer, the equivalent of a shade under 20 million gold ounces.

In COMEX silver futures, as of Feb 12, the commercials reduced their total net short position by 2700 contracts to 75,500 contracts. As was the case in gold, despite the reduction in the total commercial net short position, the concentrated net short position of the 8 largest traders increased by 1100 contracts to 101,355 contracts, the equivalent of 506.7 million ounces. The main issue remains concentration.

Of interest was the fact that the managed money traders added 4014 new short contracts (in addition to selling and liquidating 1814 long contracts). I was not surprised with the managed money long liquidation but was somewhat surprised that they added so many new silver shorts. I do believe that those added shorts were likely blown out on the silver rally that developed and will be revealed in Fridayâ??s COT report, which will cover positions as of Feb 19.

Iâ??m sure itâ??s not surprising to anyone who follows COT positioning matters that managed money short selling on lower prices inevitably results in the short covering buying that drives price rallies. Here I would direct your attention to recent developments in NYMEX platinum futures. As you may be aware, unlike the strong price rallies that occurred in gold, silver and palladium from Nov 13 thru Feb 12, the price of platinum did not rally at all and in fact finished about $50 lower on Feb 12 than it was on Nov 13. Â Over that period, there was net managed money selling in NYMEX platinum futures of roughly 30,000 contracts, an enormous amount relative to a total open interest of around 80,000 contracts.

Since Feb 12, platinum prices have rallied strongly thru today, by as much as $90, much more than in gold or silver, with the most obvious reason being short covering by managed money traders. This short covering should be evident in Fridayâ??s COT report and most assuredly in the following weekâ??s reports. Once again, it is evident that managed money selling and buying, all orchestrated and arranged by the commercial traders, are what cause the price of world commodities to rise and fall â?? as the Justice Department can ascertain with a minimum of investigation.

I would be surprised if Fridayâ??s COT report covering positions as of Feb 19, doesnâ??t indicate a further increase in the concentrated short position in both COMEX silver and gold. Once again, this will also indicate that, in the absence of this increased concentrated short selling, gold and silver prices would have increased much more than they had increased by Feb 19.

Todayâ??s selloff in gold and silver obviously conjures up the image that the either or resolution that must come will come to the downside. That may turn out to be the outcome that comes in the end, but it is still premature to know that for sure. There is no timetable for the resolution just that it will occur in time. One thing the selloff does accomplish is to temporarily reduce the open and unrealized loss of the 8 big shorts in COMEX gold and silver. As of todayâ??s close, I would calculate the mark-to-market open and unrealized loss of the 8 big shorts in gold and silver to have been reduced to just over $1 billion (based upon a 20 million oz gold and 500 million oz silver short position).

Ted Butler

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Silver – $15.66Â Â Â Â Â Â (200 day ma – $15.28, 50 day ma – $15.58)

Gold – $1320Â Â Â Â Â Â Â Â (200 day ma – $1252, 50 day ma – $1296)

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