

July 1, 2015 - The Best and Last Setup?

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I hope I have been clear in conveying just how bullish I have become over the past few weeks concerning the market structure in silver. By market structure I'm referring to the recent positions taken by the big traders in COMEX silver futures, as documented in the CFTC's Commitments of Traders (COT) Report. Of course, I am convinced that silver is massively undervalued in price based upon the actual production, consumption and amounts remaining of the real metal, but it should be clear those factors have little impact on current price movements.

Today, I intend to make the case that that the COT setup in silver is the best it has ever been in pointing to higher prices to come. Actually, that's an easy and straightforward case to make and I can do so with a minimum of verbiage. But much more important is the case to be made that the best ever setup is very likely to be the last great setup in silver. Explaining the past and present is one thing; predicting the future is another and I know the difference. So I will speak of the past and present in no uncertain terms; while I'll make the argument about the future as convincingly as I can.

July 1, 2015 - The Best and Last Setup?

That this is the best COT market structure ever in COMEX silver is just another way of saying that managed money traders (technical funds) currently hold their largest short position in history. And, as it turns out, short selling by managed money traders is also at or close to the largest historical levels in COMEX gold and copper and NYMEX platinum and palladium as well, making those markets at or close to the best market structure setup in history. (When considering all factors, however, no market comes close to the overall setup for higher prices than in silver.)

The best setup is quantified by the largest managed money short position because these traders can't possibly deliver metal to close out their short positions and, therefore, must buy back those shorted contracts at some point. The larger the technical fund short position the more bullish because it guarantees larger future buying. This is not just a theory □ there has never been an instance where the managed money traders have not bought back all or nearly all of recently added short contracts. It follows that the largest managed money short position in history would equate to most bullish setup ever. If anyone doesn't see that, please let me hear from you.

On the basis of the largest prospective guaranteed buying ever in COMEX silver, it's easy to make the case this is the best setup ever. In actual numbers of short

July 1, 2015 - The Best and Last Setup?

positions added by managed money traders over the past month, nearly 43,000 new short contracts (215 million oz) were added and that must be bought back at some point. This is the largest number of short silver contracts added on the COMEX by these traders in history. It's really not a question whether the 43,000 shorted silver contracts will be bought back and, most likely, bought back in a hurry; but how aggressive the commercials will be in selling into that guaranteed buying.

So the case for the best setup is obvious, even though we can't know how far the rally will carry once it commences and the moving averages are penetrated to the upside. But where do I get off suggesting this may be the last great setup in silver? I admit that in the past, whenever we have been in an extremely bullish setup in silver, that I have made the case that it needed to be treated as if was the final blasting off point for the simple reason that there would be little chance of getting on board (if not already fully on board with silver) if it was. And if it wasn't the final blastoff point, that would be seen at higher prices and heavy commercial selling □ and that always turned out to be the case.

I don't regret my previous takes because bottoms were made and prices did rally (admittedly rallies have gotten progressively weaker), but what I'm speaking about today is different. It's not just that every extremely bullish set

July 1, 2015 - The Best and Last Setup?

up (large technical find shorting) must be treated as if it's the big one; it's more that the circumstances around the current setup are so extreme and different from what existed in the past, that the case can be made by highlighting the differences. The whole point in identifying the last great set up is because that will be the last great chance to buy silver cheaply □ any future bullish setups will only come at much higher prices.

One glaring difference today is that JPMorgan now holds the largest privately owned physical hoard of silver in history; today larger than ever before. A little over four years ago, JPMorgan owned no silver, to my knowledge. That's when it made the decision to stockpile silver and just about every single day since, the bank has accumulated actual silver in all forms (mostly 1000 oz bars, but also including silver bullion coins from the US and Royal Canadian Mints). Combined with the recent aggressive short covering by JPM on the COMEX and SLV, I don't know how this wouldn't equate to being the best time yet for JPMorgan not to stand in the way of the next silver rally. From owning zero silver to owning 350 million+ oz - can there be a bigger difference?

Another big difference has been the growing awareness and market commentary about the price discovery process on the COMEX. Just because this has been a gradual process does that make it any less powerful. Every day,

July 1, 2015 - The Best and Last Setup?

someone new seems to recognize the market mechanics of the COMEX and comments on it. For the first time ever, mining companies have written to the regulators about this issue (a difference that still knocks my socks off and not just because they used my suggested letter).

The reason this is important is because what is currently occurring on the COMEX is a scam and fraud that cannot stand up to legitimate explanation by the regulators or anyone else. Some may suggest that argues for its continuance, but history indicates a fraud brought into the sunshine stands little chance of long life. Besides, the growing bad publicity surrounding the CME, JPMorgan and the CFTC creates a situation where something has to give □ either these institutions learn to accept the continued attacks on their reputations (never knowingly tolerated in history) or they move to end the attacks. The only ways that can occur were if these institutions address the issues directly (perhaps retaliating against the accusers) or ceasing their bad behavior. If JPMorgan stopped manipulating silver prices, then by definition, this would be the last great silver setup.

But if there is one overriding difference that convinces me that this is the last great setup in silver, it is my strong belief, whenever the last new short is added, that there will never be a time in the future where the technical funds

July 1, 2015 - The Best and Last Setup?

will hold a larger managed money short position than on this go around. This is the key. In fact, when I look back and try to explain to myself why JPMorgan never let silver rip to the upside before now, when it had a relatively small COMEX short position, the only answer I can come up with is because it knew it would be in an even better position in the future. That's the only thing that makes sense to me.

But now that the technical funds hold their largest silver short position in history and, not coincidentally, at the lowest silver price in their collective decades-long experience, what are the odds that these managed money traders will ever hold an even larger short position in the future, making this not the last great setup? Before I answer that question, let me point out why this is what will determine whether this is the last great setup.

JPMorgan, along with other commercials and now large speculators, can only buy as many silver futures contracts, in order to cover shorts or add new longs, as the managed money traders can and do sell short. There has to be a buyer for contract sold and vice versa and it is the traders in the managed money category that determine how many contracts JPMorgan and everyone else can buy. Once the managed money traders hit the limit of what they can sell short, the buyers hit the limit of what they can buy and then the rinse and repeat

cycle recurs.

The current historic 53,000+ contract short position in the managed money category did not occur by happenstance. These traders follow the price, gradually selling more on the way down and buying more when prices rise over both long and shorter periods of time. It has taken more than four years and a steady drop in the price of silver from near \$50 to under \$16 to bring about the current historically large short position by managed money traders. The only way the position could ever grow as large or larger than it is currently is if, after the next rally and when the managed money traders have finished buying back the 43,000 short contracts they just added, they can be persuaded again to go short in record amounts.

But the odds of that are remote simply because silver prices have become so depressed and have dropped for so long (4 years) that the downside looks limited from any number of practical considerations, from the cost of mining it to visceral observation that it's too cheap on any relative or absolute measure. This time around the managed money traders shorted an additional 215 million ounces in less than a month and while that did cause prices to drop almost as much as \$2 from the highs of May, it left them in a vulnerable position □ their average price on the short sales they added is around \$16, not far from current

levels.

Incredibly, the managed money traders hold their largest silver short position in history at the most dangerous (to them) low price level ever. The only way these traders could come out of their current massive short position at a profit would be if JPMorgan and all the other recent commercial and large speculative silver buyers caved in and panicked and sold on lower prices. I don't think JPMorgan is capable of caving in on anything.

I remember full well that last fall, when the managed money traders held a then-record short position in silver that the unthinkable occurred and a number of the smaller commercials panicked out of long positions at great loss and thereby enabled the technical funds to buy back big silver short positions at a collective profit of near \$400 million. I remember offering to dress up as the Easter Bunny and fly the Space Shuttle were that to occur, so I learned (again) to never say never. But the circumstances are markedly different today.

Back then, the smaller commercial longs were already deeply in the hole, underwater to the tune of \$3 per contract on close to 20,000 COMEX silver

July 1, 2015 - The Best and Last Setup?

contracts and they did panic and sell when silver dropped another dollar (to under \$15) briefly. It's much different this time. Now the massive managed money short position, as well as the corresponding long position is held with little relative open profit or loss and it is hard for me to imagine the longs panicking since they don't appear to be under any real financial pressure. It's much easier for me to imagine the technical funds shorts coming under financial pressure due to a sudden jump in silver prices. And if that occurs (as I expect), I doubt the technical funds will be looking to build up future silver short positions to the extent they have built up their current historic short position.

Having readily acknowledged that what happened last fall was completely unexpected by me, let me say that things have worked out since then as usually dictated by the COT market structure. Yes, the technical funds not only made an unexpected score last fall, some did quite well on the big price drops starting in 2013. If they hadn't done well from time to time, there is no way they would be holding their current massive short positions. That's how technical funds operate.

But it would be a mistake to narrowly focus on the technical funds' unusual profits on the short side of silver last fall and from time to time over the past few years, as these were unusual occurrences. When you take away the very

July 1, 2015 - The Best and Last Setup?

few positive scores from the short side, you are left with a much more common pattern of the technical funds generally losing on the vast majority of their forays onto the short side of silver. Netting out the technical funds' few big scores and many more losses on the short side of silver over the past four years, these managed money traders look to be a bit in the hole overall.

And away from the unexpected technical fund score on the short side of last fall, I think I've done a pretty good job of explaining and even predicting what would come next from the technical funds since then (absent the big move yet to occur). Not because I'm so smart, but because the pattern is so clear and regular. I may be tempting fate a bit here, but in the May 27 article, "Curiouser and Curiouser" (in the archives) in response to subscriber questions as to how far the suddenly negative COT market structure caused by the one week buying of 24,000 technical fund contracts might cause the price to drop, I wrote the following "

"It's more about the number of contracts the commercials can get the technical funds to sell than it is the actual level of prices or the time it takes the commercials to get the funds to sell. At this point, I see no reason why silver has to drop much more than a dollar or a bit more from current levels, say back to the lows of the year or slightly lower; all depending on how many slices of the salami it takes to get full

July 1, 2015 - The Best and Last Setup?

managed money selling. The same goes for gold, say \$40 or so to go. Of course, if the commercials really want to be vicious, prices can go much lower than that, but the offset, particularly in silver, is that much lower prices just might result in more silver miners standing up to what is already a grossly egregious COMEX price manipulation.□

On May 27, the price of silver was \$16.65 (gold was \$1187), so the managed money traders have added 43,000 contracts of new shorts on the dollar or so down that I expected. Actually, there were many more contracts added to the short side than I expected, but that's nothing but good news, particularly considering how limited the price drop was. Don't misunderstand me □ I know that these price slices to the downside feel like slices of flesh carved from silver investors, so I am not minimizing the emotional toll they take on all of us. But an objective review of what occurred over the past month should leave us jumping for joy at the resultant improvement in market structure.

The fact that we've seen an historic buildup in managed money short positions on what has been the smallest price drop of the last four years goes a long way to making my point that this could be the last great setup in silver. I can't guarantee that there won't be still lower prices in the very short term, but that looks increasingly unlikely given the historic number of managed money contracts in place already. What looks much more likely is a price explosion ahead and if we do get a

July 1, 2015 - The Best and Last Setup?

big enough lift off, then it will become obvious that this was the last great setup in silver.

There will be no COT report this Friday, due to the Independence Day holiday. Accordingly, I will have some late commentary on Monday after the new report is published, in addition to Saturday's weekly review. But considering how expertly prices have been sliced to the downside in the reporting week ended yesterday, it's hard for me to imagine how there won't be additional managed money short selling in Monday's report for both silver and gold.

More than anything else, the steady drip of slightly lower prices this week in silver and gold against the backdrop of dramatic world news (Greece, etc.) points like never before to the dominant price influence as positioning on the COMEX. Certainly, whenever silver launches upward, there will be more manufactured reasons explaining the move than can be imagined; but in reality there will only be one □ that JPMorgan decided to let it run free. That moment is close at hand according to everything I see.

Since I won't be discussing the new COT report in Saturday's review, I'll save discussion on the other developments in silver this week until then, including sales of Silver Eagles, deposits/withdrawals in SLV and the first few days of silver deliveries

July 1, 2015 - The Best and Last Setup?

in the COMEX July contract (hint □ JPMorgan is still taking deliveries in its own house account).

Ted Butler

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Silver - \$15.55

Gold - \$1167