

Weekly Review

After a two week setback, prices for gold and silver rose this week, with gold up \$28 (2.1%) and silver up by 70 cents (3.6%). Silver did manage to eke out a new weekly closing high going back nearly two years, while gold's weekly close came just shy of an even longer peak set three weeks ago. As a result of silver's slight relative outperformance this week, the silver/gold price ratio tightened in by more than half a point to just under 67 to 1, also near the highest relative valuation for silver in two years.

There were a number of truly extraordinary developments this week that need coverage and analysis. As usual, all were COMEX related and included new indications of stress on the commercial shorts in my ongoing financial scorecard, unprecedented gold deliveries and downright shocking changes in this week's gold COT report. I'll get to all these things after an abbreviated version of the usual topics reviewed.

The turnover or physical movement of metal brought into or taken out from the COMEX-approved silver warehouses cooled off notably this week as just over

2.5 million oz were moved, the lowest weekly movement in a few months. Total COMEX silver inventories fell by 1.3 million oz to 154.1 million oz. I wouldn't read too much into this week's turnover and would note we are in a "quiet" point in COMEX deliveries for silver, with COMEX gold warehouse movements (mostly in) and deliveries taking center stage.

The reason COMEX silver deliveries were quiet in July, normally a very active delivery month, was because JPMorgan stepped back from pressing for additional deliveries after taking much larger quantities for the past year and a half. In fact, JPM fell shy of the 800 contracts I expected in taking 771 silver deliveries this month, not much more than half the allowable 1500 contract limit (not that it couldn't get around the limit if silver were available). HSBC ended up as the big stopper in July with 1039 contracts of the 2474 total deliveries. Along with JPM's stepping back completely from buying Silver Eagles, I can't help but interpret this as JPM knowing how tight physical silver conditions are and/or trying to avoid contributing to the tightness.

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

First in the extraordinary development department this week is the COMEX

August gold delivery process, where after only two delivery days a total of 6829 contracts (682,900 oz) have been issued, only a handful of contracts shy of July's 6892 contract full month total. August is a traditional COMEX gold delivery month (where July wasn't), but with roughly 6500 contracts still open in August, it is safe to assume July's total will be greatly exceeded. It doesn't look like June's record of 15,785 total deliveries will be achieved or exceeded unless enough new contracts are added as August progresses. There are no signs that new contracts have been added, but two days is hardly sufficient time to get a strong feeling. (The link above contains year and month to date data on COMEX silver and gold deliveries).

Looking at some of the big issuers and stoppers for August gold so far, a few names stand out. The big gold issuer to date has been Bank of Nova Scotia which has issued 4382 contracts (after depositing the delivered gold the past few days in its COMEX warehouse). HSBC, which had been the big gold issuer for the past four months has turned stopper this month to the tune of 1382 contracts. Other big stoppers include Macquarie Futures USA (1421 contracts) and JPMorgan, with 1290 contracts stopped for a customer(s) and 316 contracts for its own house account.

I'm not looking to bog you down with the details, but rather to stress how

unusually large physical gold deliveries have been on the COMEX since April, where through today more than 35,000 total gold deliveries have been made, the equivalent of 3.5 million ounces of gold, fully a third of all the gold in the COMEX warehouses. Even acknowledging that there were quite a few redeliveries which artificially boost the total numbers, it is safe to say physical gold deliveries have been unusually large on the COMEX since April. JPMorgan for its own house account or on behalf of a client(s) has taken more than 19,000 of those gold contracts in physical delivery. It looks to me that JPM is picking up physical gold via COMEX deliveries over this time, just as it did in acquiring physical silver over the past five years.

There has been much talk over the years about a new foreign physical precious metals exchange overcoming the COMEX's paper derivatives control on price. In an ironic twist, it looks like the recent surge in physical gold deliveries on the COMEX might suggest physical pressure coming from the COMEX itself. In a sense, the recent large physical gold deliveries actually underscores the COMEX as the prime source of precious metals pricing.

While it will be interesting to observe how the COMEX August gold delivery process plays out this month, in the don't look now department, there is a record large number of contracts already open and apparently intended for

delivery in the very non-traditional September COMEX gold contract. More than 10,000 contracts are already open in September, more than were open in the July contract which resulted in more than 6800 deliveries. For the time being and in both physical and paper, the COMEX is where it's at.

Silver Eagle sales ended July at near the lowest monthly level of coins sold in years. I've read various explanations for the sharp falloff in sales and maybe I'm being guilty of confirmation bias, but the most logical explanation is that JPMorgan stopped buying these past two months after buying Silver Eagles aggressively over the past five years. In fact, I believe this month's sales of less than 1.4 million Silver Eagles is accurately representative of what retail demand has been over the past five years, rather than the exception. In other words, I believe JPMorgan may have accounted for a lot more than the 50% of total Silver Eagles sales over this time, maybe closer to 75%. That would mean JPM may have picked up closer to 150 million Silver Eagles of the more than 200 million produced over the time, and not the 100 million I previously estimated. (Plus more in Canadian Maple Leafs).

http://www.usmint.gov/about_the_mint/index.cfm?action=PreciousMetals&type=bullion

The changes in this week's Commitments of Traders (COT) Report were dramatic and unexpected when one looked under the hood. On first reading, the headline number changes looked unremarkable and fairly close to expectations, at least in gold, although the slight increase in the total commercial net short position in silver went counter to my expectations. Under the hood, particularly in gold, this was a most extraordinary report.

In discussing the report shortly after its release yesterday with Ed Steer, I had to stop and recheck my calculations to make sure I hadn't made a mathematical error of some sort. In fact, I did so again this morning. Let me run through the numbers to show you what was so unusual.

In COMEX gold futures, the commercials reduced their total net short position by 6500 contracts, to 309,000 contracts, the lowest total in six weeks and down more than 30,000 contracts from the peak four weeks ago. Still, a total commercial net short position of over 300,000 contracts in COMEX gold has to be considered a nosebleed bearish level on any historical basis. (Unless the commercials get overrun, which would then be bullish to the extreme).

Since price action during the reporting week ended Tuesday was mostly flat to down, some reduction in the commercial short position was expected. But what wasn't expected was the weekly change by commercial category, something I cover regularly. I think I may have written about this recently, but I can assure you I have thought about it constantly, as it goes to the core of my analysis.

On this week's slight reduction in total commercial shorting in gold, the big 4 actually added 8400 new short contracts and the raptors (the smaller commercials apart from the big 8) also added 1800 new shorts. Mathematically, that meant that the big 5 thru 8 bought back a very hefty 16,700 short contracts, moving completely opposed to the rest of the commercials. I joke about the commercials usually behaving like the Three Musketeers (all for one, one for all) or how they all got the office memo to buy or sell in unison each week; but it is no joke that the big 5 thru 8 behaved so radically different from the other commercials this week.

The most plausible explanation for the big buyback of gold short positions by the 5 thru 8 largest short traders is that one of these traders bit the financial dust and closed out its gold short position. Aside from a possible reporting error, I can't even come up with an alternative explanation. Certainly, I have been prepared for signs of a weak link among the commercial shorts, given the

unprecedented unrealized losses currently attached to short positions in COMEX gold and silver. And unless you were mindful and attuned to concentration data, most likely, you would not see it.

I think I explained that if a member of the small group of the concentrated shorts moved to buy back its short positions, it would be mandatory, with a capital $\square M$ that another(s) of the remaining big short sellers would have to increase its short position. Otherwise prices would soar for sure because there would be few if any other sellers. Other big shorts would have to take up the slack in order to prevent a price runaway.

If a (smaller) member of the big 8 was forced to buy back its short positions at a big loss and was replaced by a larger commercial crook, it would turn up as an increase to the most concentrated group of the big 4. If a big 4 member bit the dust, it was most unlikely any other commercial could fill the void, except JPMorgan. If JPM bit the dust, the rest of the remaining shorts should seek out the last rights.

Unless my eyes and reason have deceived me, this week's concentration data

indicate that a member of the big 5 thru 8 commercial shorts has closed out its short position and was replaced by a member or members of the big 4. If that biggest trader on the replace side wasn't JPMorgan, then I would be genuinely surprised, but should know with greater clarity when next week's Bank Participation Report for August is published. Let me finish the COT reporting before coming back to this remarkable development.

On the managed money side of the COT ledger (more than ever, there are only two sides to the gold and silver ledger – large commercial shorts and managed money longs), the technical funds were net sellers of around 5000 contracts, almost matching the headline number reduction of 6500 contracts, but only by happenstance. The only thing important about this week's COT report is the passing of a former big commercial short seller and that position's replacement by JPM, in all likelihood.

In COMEX silver futures, the total commercial net short position grew by a slight 900 contracts, to 107,100 contracts, yet another all-time bearish extreme. Unlike what occurred in gold, there was only a scant increase of just over 100 contracts in new short selling by the big 4 (and none by the big 5 thru 8). The raptors added 800 new shorts. After what occurred in gold this week, I looked extra close to see if there were signs of a big short trader closing out its position

in silver, but saw none. I'd peg JPMorgan's concentrated short position to remain at 32,000 contracts and I am anxiously awaiting next week's BPR for clarification.

The surprise in silver was in the managed money category, where traders added 5200 new long contracts, once again setting new records for net and gross long positions, just as the commercials set new records on the short side from everything from total shorts to record large concentrated positions for both the big 4 and big 8. You'll remember that the managed money traders added an unusually large 6000 longs last reporting week as well. Normally, I wouldn't hesitate to call these managed money traders the technical funds, but because silver prices didn't hit new highs in the past two reporting weeks, it is possible that the managed money traders I have previously identified in that category as core longs, but not technically oriented, may have been the buyers. However, those core non-technical fund longs have always bought on lower prices and silver prices weren't down substantially in the past two reporting weeks.

I would point out that the current record commercial short position in COMEX silver, both in total and by concentration measures is more than double what it was at the peak in silver prices near \$50 in April 2011. Here we are, down 60%

from that price peak and the commercial short position is more than twice as large today. And not one of the 8 big silver shorts who hold more than 93% of the entire commercial net short position is a legitimate producer or hedger. This is as insane and dangerous as it gets and what just transpired in gold illustrates the danger.

The only thing standing against sharply higher silver and gold prices is the resolve of the 8 big shorts in each to maintain and increase the concentrated short positions on higher prices. If these 8 big shorts fail to cap and contain higher prices from here, it would likely be game over. Should any additional members of the remaining big 8 shorts decide to cut bait and cover short positions at great loss and there not be sufficient replacement by other big shorts it would definitely be game over. And should JPMorgan not fully participate as the short seller of last resort (as it could easily decide to do), well that's the definition of game over.

I find myself thinking about the circumstances of how the big 5 thru 8 gold short which bought back its short position and came to be replaced by JPMorgan or another big short trader. This doesn't sound at all like a fully open market transaction in which a big short moved to buy back in a transparent manner and accepting free market sell orders to close out the short position. Instead, it

reeks as an arranged trade (highly illegal) in which the vast majority of market participants and observers knew nothing about as it was transacted. The price action during the reporting week it which it occurred was highly orderly and no hint was given that a big short fish was in trouble. My guess is that the big gold short which covered came into financial distress weeks ago and was carried by the exchange until the position rearrangement was finalized.

As such, someone had to know of it □ certainly the short trader which bought back and JPMorgan or whoever else added gold shorts. The CME clearing house had to know and probably arranged the illegal transaction. While I am convinced few other traders were aware of the gold short in trouble, I am not sure if the CFTC was in on this or is as out to lunch as some (including me) profess. My hunch is that the CFTC was told after the gold short got in trouble but before the transaction was effected. In any event, this was an arranged transaction in keeping with a long COMEX tradition of arranged transactions (such as the Bear Stearns takeover and the May 1, 2011 silver price massacre). The only questions are was it enough and what now?

Even though I think I have a clear reading on what took place that doesn't extend to blueprinting short term price action. As I've maintained all along, I've narrowed it down to either we go straight up from here or experience one last

hard shake to the downside before lifting off for good. This week's extraordinary big 8 gold repositioning just accentuates either outcome. Should the commercials lose control, prices will surge and it is hard to understate all the unintended consequences. I'm not an end of the world guy, but a genuine commercial failure could rock the world.

The alternative is that enough insiders appreciate the dimensions of the problem at hand that all measures will be taken to insure against a disorderly price melt up. The only "solution" that I see is that prices must be rigged sufficiently lower and soon so as to trip off sufficient technical fund selling to allow the commercial shorts to move away from death's door. I may be wrong, but I believe the imperative for the COMEX commercials is to buy back as many short positions at as close to no loss as possible and never again put on such a large and dangerous short position.

Of course, the driving force behind the extraordinary gold short buy back this week was the ongoing financial toll that has been placed on the commercial gold and silver shorts due to rising prices. The price advance this week in gold and silver added more than \$1 billion to the combined commercial unrealized loss. Further, considering that previous realized profits were of little help to the gold short which bit the dust in the current reporting week, I'm going to take

July 30, 2016 – Weekly Review

subscriber Chris' suggestion to remove realized profits from my ongoing tally.

Accordingly, I'd peg the combined open loss to the commercials short in COMEX gold and silver to be at \$3.2 billion as of last night, close to the negative extreme of several weeks ago. It's hard to imagine how many more billions of dollars damage the commercials can handle as if nothing's wrong. My hunch is not many more before the final position resolution.

Lastly, a general note that with first notice day having past for the August gold contract, a number of price reporting services (including CNBC and Stockcharts.com) have switched to the December COMEX gold contract, now the most actively traded contract. The only problem is that the December price is about \$7 over the spot price, making price misstatements inevitable but unintended.

Ted Butler

July 30, 2016

Silver – \$20.40 (50 day moving average – \$18.23)

July 30, 2016 - Weekly Review

Gold - \$1351 (50 day moving average - \$1294)