

June 1, 2013 – Weekly Review

Weekly Review

After showing upside signs of life on Thursday, prices for gold and silver fell back sharply on Friday. Gold retained slight gains for the week, finishing \$6 (0.4%) higher, while silver continued to lag and finished 20 cents (0.9%) lower. As a result of gold's relative outperformance, the silver/gold price ratio widened again to 62.5 to 1 at the very top of the trading range for quite some time. There is no question that silver has badly underperformed gold, particularly these past few months. Why is that?

To my mind, the simple answer is that silver's underperformance is no accident, but instead quite deliberate. I've always felt that silver is the weak link for the commercials in an increasing obvious gold and silver price manipulation. It is the prime candidate for physical shortage, given the limited amount of metal in existence and its heavy industrial consumption. This sets silver apart from gold. The shocking disparity between the dollar amount of above ground gold in the world (\$7 trillion) and the amount of silver bullion in industrial and investment grade form (less than \$25 billion) indicates any \hat{A} ?run \hat{A} ? by world buyers must come more easily to silver. Past history confirms this.

A little over two years ago, the silver/gold ratio was close to 32.5 to 1, as silver approached the \$50 mark while gold was priced not terribly far from where it is today. At that time, in retrospect, we were on the verge of a genuine physical silver shortage with the biggest short seller, JPMorgan, on the verge of a panic to buy back short positions. The unprecedented price smash beginning May 1, 2011, allowed the shortage to be averted, but the necessary preconditions for the shortage have not been eliminated, just merely postponed. I know it doesn't look that way today in light of the rotten silver price performance of late, but short term price performance and long term fundamental factors are not always in synch; otherwise markets would always be priced correctly with little reason for price ever to change.

My point is exactly that, namely, the rotten silver price performance has been intentional (as it has been with gold) to convince investors not to buy silver and to sell it instead, particularly in derivative and ETF forms. And considering how successful the deliberate price decline has been, there is little alternative plausible explanation to describe why silver has fallen so much given the news. Since the COT report of Feb 5, the price of silver has fallen \$10 (30%) and speculators have sold and commercials have purchased the equivalent of 220 million ounces in COMEX futures contracts alone (and perhaps double that amount when considering all other forms of silver).

Investors and speculators didn't suddenly decide in early February to unilaterally dump hundreds of millions of ounces of silver futures because of rapidly deteriorating supply/demand considerations. They were duped into it. There have been no sudden and shocking increases in silver mine or recycling production or sudden fall offs in industrial consumption; these things can't change suddenly for no obvious reason. If anything, the lower silver prices threaten to curtail production longer term. By process of elimination, the only reason for investors and speculators to dump massive amounts of silver (and gold) was in reaction to deliberately induced declining prices, all rigged by the beneficiaries of the sell-off, the commercials.

None of this is new and the only intelligent response is to recognize what has occurred and to try to position oneself in accord with the masterminds of the deliberate price smash. That means not succumbing to what the commercials want you to do.

For a holiday-shortened week and no movement on Tuesday, turnover of metal in the COMEX-approved silver warehouses resumed later in the week to maintain the pattern of the past two years. Total movement exceeded 2 million oz over the final three days of the week, as total inventories fell 1 million oz to 165.7 million oz. A reader asked how I could insist that the rapid turnover in the COMEX silver warehouses indicated physical tightness if prices have fallen so much. That's a fair question. The short answer (which I will expand on in the future) is that the silver market, like any other market, is multidimensional with many different price influences. At any time, some influences exert more price influence than others. The intentional inducement and forced sale of hundreds of millions of silver derivatives over the past few months supersede the day to day physical tightness indicated by the rapid turnover in COMEX silver inventories.

Sales of Silver Eagles finished the month at high levels, both absolutely and relative to Gold Eagles, but with no updates for the final days for the silver version. I suppose there could be a revised total given that Friday was the last day of the month and the US Mint can report erratically. There was a separate report of record sales of Canadian Maple Leaves, both gold and silver. If sales continue at the pace of the year so far, it is projected that total sales of silver coins by the US and Royal Canadian Mints will equal or exceed the combined silver mine production of both countries. So much for poor fundamentals being responsible for silver price weakness.

The changes in this week's Commitments of Traders Report (COT) were strange, to say the least. As I am travelling (this review is being written in transit), I first was informed of this week's report by phone from Ed Steer. He told me of the headline number of the total commercial net short positions in gold and silver, but then the phone connection failed and I didn't hear from him for a while. The headline numbers were that the total commercial net short position for silver was down 3600 contracts, to 8,300 contracts and for COMEX gold, it was down 24,900 contracts to 59,200 contracts.

Two weeks ago, I had estimated that as a result of the vicious price takedowns in the then-current reporting week (including the 10% Sunday night silver massacre) that the total commercial net short position would decline by 5000 contracts in silver and 20,000 contracts in gold. Instead, the next COT report showed only a 1300 contract reduction in silver and no change in gold. Last week, I analyzed that report as if it were correct, but with an eye towards there being some big revision in this week's report.

Hearing from Ed that the new report hit my two week ago estimated change exactly in silver and was very close in gold to my original guess, I couldn't help but think I had pegged the report correctly and that the CFTC was not timely in its reporting (as occurred back in April). Armed only with the headline number, I fleshed out the details of the report in my mind, getting under the hood as it were until I could verify the actual details. Then, when I reconnected with Ed to get the details, those details were as far removed from what I had imagined as were possible. In essence, this was one of the strangest COT reports in my experience. Even though the headline numbers were exactly as I thought two weeks ago, the report was screwy in many instances, so much so that I'm still unsure of what occurred.

I don't want to make this too complicated, but there was no normal rhyme or rhythm to the changes, particularly in gold. For one thing, given such big reductions in the total commercial net short positions, there was no corresponding increase in the short positions in the managed money category in the gold report (as I had expected). In fact, the tech funds bought back 9500 short contracts. Obviously, if there was a big reduction in the commercial net short position, there had to be a corresponding increase in shorting by non-commercials and that did occur. But the catch was that the increase in shorting didn't come in the managed money category (the tech funds), but in the other traders' reporting non-commercial category that together with the managed money traders comprise the total non-commercial category. (All this by the way is in the disaggregated report).

Generally, the traders in the other traders' non-commercial category are trading their own funds, rather than funds for clients as is the case with managed money traders, who are mostly CTA's (registered commodity trading advisors). Normally we don't see changes in the other traders category of the magnitude witnessed this week and it is the size of this week's changes that looks very unusual as there was net selling of around 35,000 contracts by the other trader non-commercials. That's what looks screwy, as does the decline in the short position of the swaps dealers (which are considered commercials) of 26,000 gold contracts this week.

Please remember that the reporting week covered in the current COT report covered only four trading days (due to the Memorial Day holiday) and it was generally a lower trading volume and price constrained week. This suggests there should have been minor COT changes, except as a catch up from misreporting in the previous report (which I suspected). That there were such big changes in the other traders non-commercial category, as well as big changes in the swap dealers category suggests either a category reporting error or some pre-arranged big position transfers of the illegal variety.

Therefore, it wouldn't surprise me if there were revisions to this report, although the CFTC will not be inclined to readily admit to screwing up in silver or gold, given the level of public suspicion that the agency is complicit in the silver and gold manipulation. Make no mistake Â? I want the headline numbers to be accurate as reported, not just because they fit my predictions, but because they are bullish beyond description. It's just the stuff under the hood looks squirrely.

Pending any revisions, I'll analyze this report as if it were correct, as is my custom. After all, there are many different calculations that go into a COT report other than trader classification by category. For instance, for the purpose of guarding against undue concentration and manipulation (not enforced in silver), every COT report indicates the contract levels held by the four and eight largest traders on the long and short sides of every market each week, regardless of category or whether the largest traders are commercials or non-commercials. This is where I get my figures for the big 4 and 8 and the raptors, as well as keeping up with what JPMorgan holds. This data shouldn't be affected by category misreporting.

The CFTC doesn't report this concentration data by actual numbers of contracts, but by giving precise percentages of the total open interest of each market held by the four and eight largest traders. It just takes a few seconds to convert the percentages listed into the precise number of contracts with the use of the simplest electronic calculator. For example, it is easy to derive this week's net short position of the big four on the short side of gold futures by multiplying the total open interest of 411,001 contracts by the percentage listed (21.4%) to get the number of contracts (87,954). Let me run through this week's report in the customary manner.

In gold, the total commercial net short position (previously stated) declined by 24,900 contracts to 59,200 contracts, the lowest such reading in many years. As such, gold is configured more bullishly than at any time in recent memory. Even if this current report is revised and the total commercial net short position is adjusted upward, the COT structure would still be strongly bullish. I say that because, in addition to unusual category changes above, there is still more strangeness to report as relates to the changes in commercial categories normally discussed.

Even though there was a reduction of 24,900 contracts in the commercial net short position, the big 4 position of 87,954 contracts (listed above) represented an increase in their short position of 6300 contracts from the previous week. In addition, the big 5 thru 8 gold shorts sold more than 3200 additional contracts short. That means the gold raptors had to buy an impressive number of new long positions to make the numbers balance. And that certainly was the case as the gold raptors net long position jumped by an incredible 34,500 contracts to a new record high net long position of 75,200 contracts, the largest one-week jump in memory. So, the big 4 and big 8 sold short 9500 additional short contracts and the gold raptors bought 34,500 contracts. And all this occurred on a nothing pricewise holiday shortened trading week. That's screwy and adds to my concern about the report being so as well.

It wasn't as screwy in silver, as at least the managed money shorts didn't buy back a bunch of shorts as was the case in gold. But neither did they add many new short positions as I had expected. As mentioned two weeks ago, if my estimate that the total commercial net short position declined by the amount as published we would be at the lowest levels of commercial shorts not seen in a decade or more. The total commercial net short position of 8300 contracts puts us at those levels. The 3600 contract reduction this week in silver, as was the case in gold, was strictly a raptor affair, as the smaller commercials accounted added 5300 new long contracts, up to a new record level of 41,700 contracts now held net long. As was the case in gold, but to a much lesser extent, it was mostly changes in the other reportable traders' non-commercial category that accounted for the 3600 contract total commercial net short reduction.

The big 4 (read JPMorgan) added 1600 contracts of new shorts. I would estimate JPMorgan's concentrated short position in COMEX silver to now be 20,000 contracts (100 million oz). I still believe JPMorgan has fully hedged this short position with actual silver (purchased from SLV liquidation, primarily) and with long silver derivatives in the OTC market purchase on the deliberate sell-off, as well as massive long metal and gold derivatives positions. But I can't help noting that JPMorgan's silver short position is almost two and a half times the 8300 contract total commercial net short position. And the short position of the big 4 is more than four and a half times the total commercial short position. Even with the record low commercial net short position, the concentrated holdings of JPMorgan and the big 4 are nothing but extraordinary. As was the case with gold, were the silver COT report to be revised, it would still remain in the strongly bullish range.

Potential revisions aside, the extremely bullish COT structures in gold and silver will be resolved at some point, probably fairly soon. Because the downward price manipulation has been so extreme in price and has lasted so long there will at some point be a crossing of price above the moving averages, either by price increases or the certain mathematical decline of the moving averages lower over time, or some combination of both. We danced on the 20 day moving average in gold on Thursday's price highs and touched that level in silver as well. The 50 and 200 day moving averages are more important and they will be violated in time, although further short term price declines will delay the inevitable.

Given that complete violation of all the important moving averages for both gold and silver to the upside must occur at some point, it is not wishful thinking to contemplate what will happen at that point. Based upon the historical record, we know that as the price penetrates the moving averages to the upside, technically established speculative short positions will be bought back. That's why any build up in speculative short positions is considered bullish ultimately. As speculative short positions are bought back and new speculative long positions are attempted to also be purchased due to rising prices, the attention turns to the sellers. We know those sellers will be of the commercial variety, based upon the historical record and accepted market dynamics. What we don't know is how aggressive the speculative buyers and commercial sellers will be relative to each other. The relative aggression will determine how prices move at that point.

If the commercial sellers are fairly aggressive, the price rise will be relatively subdued. If they are not too aggressive on the sell side, prices will move higher much faster. The two key commercial sellers in silver will be JPMorgan and the raptors. JPMorgan's importance centers on whether they add new short positions on rallies over the key moving averages. If they do add silver shorts, prices will be much more contained than if they don't add shorts. As far as the raptors, they are very likely to sell out long positions on price rallies based upon their past record. But historically the raptors haven't sold until they have a profit, no matter how long they must wait. That means they will likely sell out long positions purchased at lower prices on moderately rising prices, but will be much less likely to sell long positions on rising prices unless they become profitable.

In simple terms, there is a likely potential clash between how many contracts the speculators will be looking to buy in silver above the 50 and 200 day moving averages and how many contracts the raptors will be willing to sell, since the raptors own a bunch of contracts near \$30 or so. If the raptors don't sell sufficient quantities and JPMorgan doesn't aggressively add short positions, prices could pop to near \$30 in a flash. That may seem a great distance from here, but as I indicated earlier, we were at \$32 a few months ago and there was no legitimate supply/demand reason for why we are at \$22 today.

I suppose if one were to believe that it was the speculators in full control and not the commercials, none of this line of thinking would sound plausible. But if it were true that the speculators ruled over the commercials there would have been little validity to the COTs for the past many years. Even those who comment on the COTs but deny a silver or gold manipulation exists for the most part still label the current set up as strongly bullish. They wouldn't do so if they thought it was the commercials behind the eight ball.

Ted Butler

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Silver – \$22.15

Gold – \$1392

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