June 10, 2020 – Continued Anomalies

There have been a number of anomalies, or unusual developments in gold and silver over the past two months or so which I've discussed, but the developments have hardly been fully explained. I doubt very much that this will be the end of the discussion, as the developments are incredibly new and unusual. The developments do seem to be connected, so please allow me to put them into the sequence that makes the most sense to me. Let me present the facts first and then opine about what these facts may mean.

Starting at the very end of March, immediately following what was one of the sharpest price selloffs and snapbacks in history for gold and silver, spot or cash prices for gold began trading at a pronounced discount to the lead COMEX futures month. Silver later followed this pattern. The discounts of spot metal to futures have moderated, but still exist. This price configuration is not something I've ever witnessed, so naturally I'm very interested in uncovering the explanation.

Most of the published explanations for the discount of spot metal to futures in gold were focused on some type of disparity between gold in London versus New York and physical metal not being in the proper location for delivery. But, ironically, these explanations described why spot should be trading at a premium to COMEX futures, not a discount. Later, as the discount of spot metal to futures appeared in silver, it was no longer an anomaly unique to gold, although the reasons for the discount were still muddled and whatever the reason, the circumstances in silver appeared quite different from what existed in gold. For instance, there was no talk of silver bars being unavailable in New York versus London, as seemed to be the case in gold.

Also starting at the very end of March was the beginning of what has turned out to be a massive inflow of physical gold into existing and newly designated COMEXapproved warehouses. So massive has this flow of physical gold been that, in little more than two months, total COMEX gold inventories have risen by 3.5 times, from 8.5 million oz to 29.4 million oz so far, making the COMEX depositories now the second largest repository of visible gold inventories in the world, behind the largest gold ETF, GLD, which holds around 37.5 million oz (of course, I'm leaving out central bank holdings). I'll mention now that there has been absolutely no increase in COMEX silver warehouse inventories over this time, but come back to this later.

In addition to the massive increases in COMEX gold warehouse inventories, there has been a stunning increase in the number of deliveries against COMEX gold futures contracts, starting with the April contract and continuing through the May and June contract months. Obviously, there is a direct connection between the recent record increase in both COMEX gold inventories and the record deliveries on COMEX futures contracts. By the way, nearly 9 million oz of total deliveries have been made from April thru June so far against the 21 million oz increase in COMEX gold inventories, with both deliveries and warehouse inventories still increasing.

Certainly, both the massive increase in COMEX gold warehouse inventories and deliveries qualify as anomalies. As already indicated, there was no increase at all in COMEX silver warehouse inventories over this time and deliveries against silver futures were fairly high for May (a traditional silver delivery month) but not particularly high for April and June (both non-traditional delivery months). Therefore, the anomalies in gold inventories and deliveries are much more extreme than have been the case in silver. Yet, both gold and silver share the price anomaly of having discounts of spot to futures.

Considering the matter of the massive increase in COMEX gold inventories which increased by three and a half times, it's hard for me to even conceive of COMEX silver warehouse inventories possibly increasing by that much. Currently, the COMEX silver inventories are the second largest visible stockpile in the world at 314 million oz, behind only the holdings in SLV (473 million oz). And there are no known central bank silver holdings. For COMEX silver inventories to increase by a factor of 3.5, that would put total COMEX silver inventories at 1.1 billion oz, an increase of almost 800 million oz from current levels.

Considering that JPMorgan's silver hoard of one billion oz must be reduced by 250 million oz for what I believe it holds in its own and other COMEX warehouses and by another 100 million oz for what I allege it loaned out over the past two months, that only leaves around 650 million oz JPM could move into the COMEX warehouses, assuming no logistical restraints (of which there would undoubtedly be plenty). So even if JPMorgan chose to move every single ounce of silver it was capable of moving into the COMEX warehouses, it wouldn't add up to the 800 million oz necessary to match the same increase that just occurred in the COMEX gold warehouses. Besides, if 800 million oz came into the COMEX silver warehouses, then every ounce of the 2 billion oz of the world's silver in 1000 oz bar form would be visible and recorded. Where am I going with this?

Where I'm going is here – the recent stunning increase in COMEX gold inventory of 350%, from 8.5 million oz to more than 29 million oz, raised the total amount of gold bullion in visible and recorded form to around 141 million oz (excluding official and privately held, but non-visible and recorded gold bullion). But we know there are 3 billion oz of gold bullion in the world, out of the total 6 billion oz known to exist. So all the gold bullion in visible and recorded form, essentially the 141 million oz of gold in the world's ETFs and COMEX holdings combined, comes to less than 5% of the 3 billion oz of total gold bullion in the world.

Contrasting that with silver, the current near 1.3 billion oz in the world's silver ETFs and COMEX warehouse holdings combined, comes to nearly 65% of the total 2 billion oz thought to exist in world silver bullion inventories (all 1000 oz bars). After the massive increase in COMEX gold inventories, visible world gold bullion inventories make up less than 5% of total world gold bullion inventories. Before any potential increase in visible world silver inventories, these visible inventories make up nearly 65% of total world silver bullion inventories. What can we conclude from this?

The main conclusion, it seems to me, is that gold has such an extremely high dollar value per ounce, that holding it in visible and recorded stockpiles is mostly unnecessary except in very large quantities. One hundred ounces of gold, or about 7 lbs., is worth $170,000, a fairly sizable sum to most people in the world, and an amount most people would be quite capable of storing privately. A comparable dollar amount of silver would equal around 10,000 ounces, or 700 lbs., an amount few could lift, to say nothing of storing privately.

My conclusion, therefore, is that the reason so little gold is held in the world's gold ETFs in percentage terms and so much silver is held in the world's silver ETFs, is because you get so much darned silver for your money that you have to have someone store it for you. Let me veer off for a moment, before returning to the anomaly theme – remember, we are still looking for the explanation for the anomalies.

A good number of years ago, just after the SLV, the big silver ETF, was introduced in 2006, my good friend, Carl Loeb, coined the term "Death Star", the fictional massive galactic super-weapon from the movie, "Star Wars" that could pulverize all before it, to describe the SLV's ability to absorb all the silver that existed. In fact, years earlier in public comments to the SEC, which was seeking public input on whether to allow the ETF to come to market, I opined, without using the term Death Star, that the SLV would gobble up all the silver in the world and distort the market. Fortunately, the SEC didn't listen.

Therefore, it's no real surprise that today, 14 years after the debut of the SLV, the trust holds more than 470 million oz of silver, the largest stockpile of silver in the world, nearly a quarter of all the silver bullion thought to exist. And this is after 9 years of a distinct down market, courtesy of the crooks at JPMorgan. Had the price of silver not been manipulated downward since 2011, undoubtedly, there would be much more silver in the SLV by now. Remarkably, there is now a lot more to report, namely, that the original silver Death Star, SLV, has spawned offspring, in the form of other silver ETFs, which also appear intent on gobbling up all the silver bullion in world. Combined, the silver ETF offspring now hold slightly more than the mother Death Star, SLV, or 490 million oz. Altogether, SLV and all the other silver ETFs hold a collective 965 million oz, or close to half the entire 2 billion oz thought to exist.

To give you a sense of how tightly are held the world's 2 billion oz of silver bullion, I don't believe JPMorgan holds much, if any of the 965 million oz in the world's ETFs, but do believe it holds most of the silver held in the COMEX warehouses plus another 750 million oz in unreported inventories, mostly in London. JPM's actual holdings might be 100 million oz less than that as a result of it leasing out that amount recently, but it still holds title to that leased metal. In essence, the silver ETFs hold half of the worlds above ground silver bullion inventory and JPMorgan owns the other half. It doesn't get tighter or more closely held than that.

That so much of the world's silver is held by investors in ETFs is remarkable considering the price has barely budged above the $20 mark for six years. That so much silver is now held by investors in such a dismal price environment, makes one wonder how much collective investor demand might emerge when prices get going to the upside and investors resort to buying just because prices are rising, as seems inevitable. Invariably, these new investors will pile into the various silver Death Stars.

Here's a thought you might care to ponder – what do you think will happen, if, as and when the tens of millions of millennium hot shot day traders at Robinhood and other no-commission discount on-line brokers take a shine to silver ETFs? If they can cause the stock market and even bankrupt stocks to soar to unimaginable levels, what crazy valuations do you think they could drive an asset with real value, like silver, to?

Back to the anomalies and what explains them. Seeing as there are vastly different underlying conditions in gold and silver, namely, that gold has had massive COMEX warehouse physical inflows and deliveries against futures (and large, but more modest ETF inflows), while silver has had no increase in COMEX warehouse inventories, moderate deliveries against futures, yet absolutely massive ETF inflows; it follows that the explanation for why both experienced the unprecedented discounts in spot to futures must be different.

First in gold, it appears to me the big discount for spot metal to futures was mostly due to the plight of the big shorts, some of which chose to bring in metal in order to make delivery against their short futures contracts to close those contracts out to avoid growing open losses. Other big shorts have chosen to buy back their open short positions. Each new COT report should indicate how this short close-out process develops. The process of delivering physical metal (all things being equal) depresses spot prices, while the buyback of short futures positions elevates futures prices. While simple, this goes a long way to explaining the discount of spot to futures in gold.

On Saturday, I mentioned how speculators in the managed money and other large reporting trader categories were on the receiving (stopping) side of the gold deliveries. I still feel that way, but afterward I remembered something that might explain this more fully. A couple of months back, when the gold spreads first blew out to unprecedented discounts of spot and nearby futures to more deferred months, I tried to explain how impossible this was because the discounts were so wide that it would tend to draw arbitrage money from the moon to take advantage of a guaranteed money market return the unprecedented discounts offered to “cash and carry” spread traders. It dawned on me after sending out Saturday’s article, that this was the likely reason for the speculators taking the gold deliveries put out by the big commercial shorts.

The important takeaway, of course, is that given the efforts the big gold shorts are demonstrating in closing out their open short positions in the only two ways possible (deliveries and buybacks), a reasonable person has to ask him or herself what are the odds these same shorts will likely ever sell short aggressively again? I’d peg the odds as close to the same as for a cat who just jumped on a hot stove repeating the act.

In silver, however, there were markedly different circumstance than there seen in gold, yet spot silver prices also traded at a steep discount to futures. The most plausible explanation for the discount of spot to futures in silver is still the leasing of metal by JPMorgan, so I’ll not re-litigate the matter here. Yes, the leasing of metal temporarily depresses the price, same as in a straight sale; but whereas a straight sale is final and a closing transaction, leasing is very much an opening transaction and the metal must be returned (bought back) at some point. It is the returning of metal or the buying back that is bullish.

Turning to other matters, following what turned out to be a rather bullish COT report last week, since prices for silver and gold were higher and we didn't get the degree of managed money buying and commercial selling is silver that was expected and the opposite of that in gold, what to expect this week since prices fell in the reporting week ended yesterday should be managed money selling and commercial buying. In fact, gold fell by as much as $60 and silver by as much as 85 cents at the extreme price lows of the reporting week. Moreover, gold penetrated its 50 day moving average to the downside for the first time in more than two months and closed below that average for three of the five days of the reporting week.

Normally, such price action would argue for substantial managed money selling and commercial buying, but changes in total open interest over the reporting week were mixed with gold open interest featuring virtually no change and silver open interest increasing by nearly 6000 contracts. Also perhaps moderating big improvements in market structure is the fact that the market structure in gold was already the best it had been in a year going into this reporting week and considering how little the market structure in silver had deteriorated on the sharp $6 rally from the March lows also might moderate big improvements in Friday's report. I guess what I'm saying is that I expect positioning improvements, but am too much of a girly man this week to predict by how much.

As far as the financial standing of the 8 big shorts in COMEX gold and silver, last week they enjoyed substantial relief on the sharp decline in gold and silver prices, but still ending the week in the hole by $6.8 billion, comprised by $1.2 billion in realized losses and $5.6 billion in open and unrealized losses. At publication time, the gain in prices this week added to their overall losses by around $1.2, bringing the total losses to $8 billion ($1.2 billion in realized losses, plus $6.8 billion in open and unrealized losses) – by my recollection, the most extreme losses yet. Couldn’t happen to a better bunch of crooks.

Ted Butler

June 10, 2020

Silver – $18.20   (200 day ma – $17.03, 50 day ma – $16.13)

Gold – $1735   (200 day ma – $1577, 50 day ma – $1712)