From Here to There

I'll try to cover two new insights today, the first dealing with the short term and the other just beyond the short term. The first has to do with some general observations about the Commitments of Traders (COT) Report. It dawned on me that there is something special about the increasing attention and commentary surrounding the report I never quite noticed before.

There are a good number of different methods in which to anticipate the future price of any investment asset, both in the short term and long term. By broad category, however, it narrows down to two basic approaches technical or fundamental analysis. I'll define technical as any approach relying on price movement in some form and fundamental as relying on an interpretation of all available supply and demand data. By and large, chartists and technicians focus on the short term, while those studying the fundamentals look longer term.

Interestingly, I would consider discussions around the COMEX market structure, as defined by the COT report, to be separate from either technical or fundamental analysis; although analysis of the report is generally shorter term

by nature.

Although I am not a chartist or technician at heart, I "study" the charts fairly intensely and it would be hard not to, since such commentary makes up a large component of what is written about gold and silver. Besides, a price chart is like a picture containing a thousand words. One would think technical analysis, since it is based upon price and price change alone, would be highly objective and one unified opinion about future price would emerge. But, I suppose, if a chart tells a thousand words, it may tell a different thousand words to whoever may be studying the same chart.

In other words, ask 100 different technicians to predict future price and you might get close to a hundred different predictions. This also seems to be true when applied to a specific technical discipline, like Elliot wave analysis. Please don't interpret this as me insulting any technical approach, I'm just observing there is generally more disagreement than agreement among technicians about future price movement. At the very least, there is rarely an overwhelming ironclad consensus among those who view the market through technical eyes.

This lack of consensus is even more obvious among those using a fundamental approach to predict future price (where I would categorize myself). Considering the nearly infinite number of ever-changing actual data points that could affect gold or silver prices, the fundamentalists rarely agree as a whole and even disagree about which data points should be considered in the first place. And should a large number of fundamental analysts happen to agree on the broad levels of future prices, that doesn't mean you should rely on it. Here's a case in point the consensus of 25 gold and silver fundamental analysts as compiled just a couple of months ago by the LBMA.

http://www.lbma.org.uk/assets/Forecast_2016_Interactive.pdf

On average, the consensus on gold's price a year hence was for a 1.1% rise from the mid-January level of $1091. Instead, gold jumped more than 15% in little more than a month. Also, the average consensus high for gold ($1231) has already been exceeded. I'm not picking on these or any other fundamental analysts I am just highlighting that, like technicians, they generally differ in future price predictions and even when they agree, that is no guarantee.

Now compare what exists, namely, general disagreement among technicians and fundamentalists alike, with what exists among those that analyze the COT

report and the COMEX market structure which is complete agreement that the current market structure in gold and silver is extremely bearish. It doesn't matter that these COT analysts are worlds apart from each other on just about everything else and have even written disdainful personal things about one another; I have yet to read a recent COT analysis by anyone that doesn't expect lower prices ahead. And while I speak in terms of probabilities and not certainties, I hope I've conveyed that I feel that way as well.

My point is not whether the rock-solid bearish COT consensus that currently exists actually plays out as expected (as will only be determined in the fullness of time), but that the remarkable consensus even exists in the first place. Yes, there are always those who expect an eventual overrun of the commercials when they are heavily short and this not only is this possible, but is basically Izzy Friedman's Full Pants Down premise. I certainly expect a coming day when the COTs matter little. But my first insight today is that current COT commentary is uniformly bearish, even while there is no consensus on future price from either the technicians or the fundamentalists. Why is that so?

I believe that the reason there is such uniformity in COT analysis is because it has largely stood the test of time, particularly when compared to general technical or fundamental analysis. I'm hard-pressed to think of a time (over the

decades I have been studying the report) when after a very bearish market structure was formed that gold or silver prices surged higher amid noticeable commercial short covering. Likewise, after an extremely bullish market structure was created by heavy technical fund selling, I can't recall prices not eventually rising. Admittedly, when the COT market structure is neutral, anything can happen pricewise, but I'm speaking of extremely bullish or bearish market structures.

The main reason there is such uniformity in COT analysis currently is because there has been a remarkable historical correlation between extreme readings in the market structure and what happens to gold and silver prices afterwards. It's natural to look for correlations anywhere one can find them. Many insist there is a correlation between gold and silver prices and changes in the dollar, the stock markets or oil and other commodities. I have trouble with those other correlations, but not with the COT correlation with price when the market structure is extreme. That's not to say that prices can't go significantly higher after an extremely bearish structure is formed, just that it hasn't happened yet. The next time will also be the first time.

To my mind, the correlation between gold and silver prices following extreme market structures is the most glaring correlation of all. And I am confident those

that write about this currently have made that correlation connection themselves. Let's face it □ market analysis, like anything else, will tend to center on what has worked rather than on that which doesn't work as well. For shorter term price movements in gold and silver, the correlation between prices and COT extreme readings has worked best of all. That's why so many are writing about it.

While I have been keenly aware of the almost impeccable historical correlation between gold and silver prices following extreme market structure readings for many years, that awareness is multiplying. I think that's constructive because it leads to a deeper understanding of what moves price. What determines gold and silver prices in the short term has been futures contract positioning on the COMEX between the commercials and the managed money traders. It is close to impossible to study the COT reports and not see, in time, the dominant □ and I would say □ manipulative influence wrought by technical funds and commercial banks.

While COT considerations play out in the short term, that's not to say they can't affect the long term too. With more grasping the market structure approach daily, the good news may be the long term impact this type of new thinking has on future prices, particularly for silver. Once educated to the control that

COMEX positioning has on price, it's not hard to see that silver prices are set in a funny way a way that bypasses actual metal fundamentals and centers on purely speculative paper trading.

The best thing about the growth in COT commentary may be that it provides the best explanation for why silver prices are so cheap because its price is set artificially on the COMEX. The strong correlation between short term price and extreme COT readings, even if you are a long term investor, sets a mental image that becomes ingrained over time. Simply put, the more you study market structure, the more convinced you must become that silver is massively undervalued. It doesn't hurt that the artificial pricing on the COMEX is compatible or not in conflict with every other factor that I find most important in silver, including COMEX silver warehouse turnover, other signs of physical tightness and JPMorgan's massive acquisition of actual metal.

Just as more observers than ever are awakening to the price correlation record of extreme COT readings, as demonstrated in the current uniformity of opinion, there are likely to be other consequences like the impact on collective future silver investment behavior. An interesting email exchange with a subscriber led to this second insight. Brandon wrote about the cumulative impact on the collective mindset of silver investors from all that has been written on silver

over the past 10 to 15 years.

It has been over this time that there has been a literal explosion of alternative information on silver (and gold), unlike any other time in history. I would define alternative information as being Internet based, as opposed to more traditional main stream media information. No doubt the Internet played a massive role in the investor information explosion. The point is that alternative information delivery sources have come to lead the way in information delivery. For instance, there is no doubt in my mind that the more established media outfits, including brokerage firms, started commenting of COT reports after following the lead of what was being said on alternative Internet sites. (And yes, mine is an alternative information source).

What Brandon impressed on me was that the collective mindset of today's silver investor is very different from the collective thinking that existed before the year 2000. Even though I became focused on silver and its manipulation long before then, I include myself in that category. What I've been able to confirm or learn since the turn of the century has only convinced me more of silver's destiny with shockingly higher prices. I may take some personal measures in the face of an extremely bearish COT market structure, but at the same time always envision even higher prices when the physical shortage hits.

What this means is that the silver investors who have grasped the whole story and which are growing in number, the collective resolution not to sell except at much higher prices has grown strong. I know that's true in my case. My reason to hold silver is still as an investment I will sell someday at a very high price; it's just that, because of the continuing flow of data, my intended sale price keeps getting ratcheted up. This makes me and, I think many others, much stronger silver holders. What I took from Brandon is that, aside from the baptism of fire that declining prices over the past five years that have hardened those investors who have held, the information flow has forged even stronger hands.

In other words, those holding silver today may be the strongest silver holders ever, simply because their price expectations have grown so high. And it's not just high prices it's the physical shortage resolution to come. I'll probably end up selling too soon, but it won't be before a physical shortage mania is in full force. There's not that much silver in the world in the form that matters (1000 oz bars) to start with, say 1.3 billion oz worth no more than $20 billion and Brandon has persuaded me those holding it may be a lot stronger than I imagined.

Of the 1.3 billion oz of industry standard silver bullion that exists in the world, I am further convinced that JPMorgan has accumulated a third of those ounces over the past 5 years, or more than 400 million oz. I would consider JPMorgan the strongest possible silver hand of all. Between JPM and the assorted other world holders of actual silver (including what's in the ETFs and warehouse inventories), I believe only the slightest amount may be available to the market at anywhere near current prices. Further, when higher silver prices do come, it's even easier for me to imagine new buyers completely overwhelming old sellers and for silver to remain tight to the point of being unavailable until prices are high enough to discourage new buyers and convince holders, like myself, to say goodbye to silver forever. Just to be clear, I'm not talking about $50 or $100 silver.

There haven't been many stark new developments since Saturday's review, but the news flow continues to point to physical tightness. The US Mint still appears to be selling all the Silver Eagles it can produce with a big buyer being responsible for the continuing weekly sellouts. In essence, this has been the story for much of the past 5 years. Gold Eagle sales do seem to be trailing off and are running about half the sales pace of prior months, at least through yesterday. I'm mindful of a pattern I have attributed in the past to JPMorgan, namely, of the bank backing off from Mint purchases just before prices are smashed due to an extremely bearish COT market structure. Then, when new

low price levels are achieved, Mint coin buying magically reappears. The COMEX price manipulation and JPMorgan are part of everything.

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

The situation in the COMEX March silver delivery process continues along the lines it had been running, namely, with JPMorgan stopping (taking) as much physical silver as it can in its own name, while at the same time backing off and selling as many remaining March contracts as it must to keep prices in check. Talk about threading the needle. As of last might, JPMorgan has, once again, emerged as the leading stopper of silver deliveries in its own proprietary of house trading account, as it did all of last year. This month, JPM has stopped through yesterday, 483 silver contracts (2.4 million oz) in its own account of the total 725 silver contracts issued. But the total level of deliveries is somewhat misleading, as a customer(s) of JPM started delivering yesterday after stopping deliveries earlier in the month, making the JPMorgan proprietary trading account the largest taker of silver deliveries this month by a greater level than the numbers might suggest.

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

With only 700 contracts or so still remaining open in the March futures contract, it's hard to see JPMorgan acquiring more than 1000 contracts in total this month. Since JPM and its customer(s) were in position to accept 3000 contracts at the start of the delivery month, having to miss out on acquiring another 10 million oz of physical silver (2000 contracts) had to hurt a bit, but by not pressing the March shorts for physical delivery, JPMorgan pushed off further delivery tightness. This was clearly intended to make it easier for the crooked bank to rig prices lower in the hopes of buying back many more of its short contracts. JPM is the kingpin in silver futures and physicals and knowing that makes everything easier to understand, particularly why silver prices will end up much higher than most could imagine because it will benefit JPM.

With yesterday's cutoff for the COT report to be reported Friday behind us, I wouldn't imagine dramatic changes in the new report. Total open interest is marginally lower from the prior reporting week and price action was mostly choppy to lower in gold, with prices ending the reporting week down about $30, and less so in silver. If I had to guess, I'd say a slight improvement (a lower total commercial net short position) in each, but that's only if I had to guess.

Gold and silver prices did jump late today (more than 2%) after the Fed's announcement, but I haven't attributed precious metals movements to Fed actions over the past few decades and I am disinclined to start now. Despite the late surge today, gold and silver prices are still within the broad trading range of the past 5 weeks or so. Gold and silver can certainly make new highs for the move, although I have difficulty in seeing prices advance strongly from here for the same reason we rose so strongly into mid-February, namely, massive technical fund buying in COMEX futures.

It's also important to remember that the COMEX commercials do not appear to be under any financial stress yet due to higher gold and silver prices. Contrary to popular belief, the commercials made out like bandits on the big surge in gold prices this year in selling out long positions (by the raptors) while the technical funds got hammered in buying back short positions at big losses. The technical funds are now firmly entrenched on the long side with the commercials big net short, but my guess is that the technical funds have gotten big net long in gold at an average price of around $1230 in gold and $15.40 or so in silver. It would take big price advances from here ($100+ in gold and several dollars in silver) to put the commercials under pressure or even to erase the gains they made this year. That is certainly within the realm of possibilities of course, but not yet within the likely probabilities.

Ted Butler

March 16, 2016

Silver – $15.60 (50 day moving average – $14.78)

Gold – $1260 (50 day moving average – $1173)