Weekly Review

The sharp price spike that occurred late Wednesday and into Thursday on Federal Reserve developments (whatever those developments were) was sufficient to result in higher weekly closes for both gold and silver. Gold ended $4 (0.3%) higher and silver finished up 29 cents (1.9%), its highest weekly close in five months. As a result of silver's relative outperformance to gold this week, the silver/gold price ratio tightened in by one and a half points to 79.5 to 1.

This is the least undervalued silver has been relative to gold in several weeks, but silver is still so massively undervalued by this measure that short term changes of even five or ten points in the price ratio are meaningless. It's true that the longer a price or a price ratio remains at even the most preposterous level, the more that level appears reasonable. I suppose it has to do with getting used to anything if it lasts long enough. I believe that's the case for silver, both in terms of its current price and its price relative to gold (and just about everything else).

But if the current price of anything is seriously out of kilter with what the

underlying facts say it must be, the price will adjust to the proper level in time, no matter how accustomed we get to the current price level. In the daily and weekly churn in price, the price itself becomes the focus, often to a point where real valuation is overlooked. This is the whole point behind analysis trying to uncover mismatches between value and the current price. Simply put, I doubt there has ever been a greater mismatch between value and the current price than is the case in silver, both in its absolute and relative price level.

In fact, there are no facts supporting the current absolute and relative price levels in silver, at least no legitimate facts. The actual physical situation in the wholesale silver market has rarely been tighter or promised to get even tighter in the future, as evidenced in the verifiable data I cover on these pages. That leaves the only explanation for price the paper positioning changes in COMEX futures contracts. This week was a case in point.

Gold prices jumped more than $30 within minutes of the Fed's announcement late Wednesday and then the real trading volume came in. There was no other world gold market even open for trading at that time other than the COMEX, so, at least in this instance, it's easy to declare Wednesday's price ramp to be an exclusive COMEX production. In actuality, it's always an exclusive COMEX price production whenever the price of gold or silver move, but in this case there can

be little argument since no other market was open. For some unknown reason, the paper games this week on the COMEX resulted in silver gaining, both on its own and relative to gold.

My point is that price of gold, silver and the silver/gold ratio is dictated by paper contract positioning on the COMEX and little else. I couldn't begin to explain why prices moved as they did this week or any week in the absence of the COMEX explanation. And since there is no way to predict in the very short term how the daily battle between the commercials and the speculators (mostly technical funds) will play out on any given day, except by the broadest probabilities, I don't even try.

Because the daily COMEX paper positioning drama has little to do with the actual metal facts in the world of silver, a great disconnect has resulted in which the current price has become incompatible with the actual metal realities. It is this disconnect that is both so frustrating because it has lasted so long and so enticing to long term investors because it represents an artificial undervaluation for the history books. The more undervalued an asset becomes to its fundamental value, regardless of the cause, the better an investment it becomes. While it is possible for silver to become even more undervalued in the short term due to COMEX positioning, it is currently undervalued so massively

that any potential weakness in the short term will be forgotten in time.

After nine weeks of absolutely torrid physical turnover of metal brought into or taken out from the COMEX-approved silver warehouses, which averaged 8.5 million oz weekly, this week's turnover amounted to just over 2.8 million oz, as total COMEX silver inventories fell by 0.5 million oz to 155.1 million oz. I would point out that this week's movement, when annualized, is still around 150 million oz and if my contention is correct that there are only around 15 million oz in true available COMEX working inventory, then this week's □slowdown□ still represents an annual turnover of ten times working inventory □ a level unheard of in commodity terms and highly suggestive of physical tightness.

This week's COMEX silver warehouse turnover brings us back to the former levels of weekly inventory movement before the explosion in turnover the past two months. Something is behind the unusual turnover which has now lasted for five years and I still maintain it is directly related to physical tightness. This COMEX silver turnover started in April 2011 when silver spiked to nearly $50 and when JPMorgan opened its own COMEX silver warehouse, which subsequently become the largest COMEX silver warehouse of all. I would contend there is nothing coincidental about this and will devote a separate article soon on the role of JPM in silver these past five years. There's not enough

time today, but the story of silver for the past five years is the story of JPMorgan.

I never predicted that the COMEX silver warehouse inventory would begin to turn over frantically or that it would remain continuous for five full years, because that would have been impossible. I just report the movement after it has occurred. Most amazing of all is how unnoticed and underreported it has remained to this day. We've seen the turnover dramatically speed up recently (until this week), but the key feature to me is its consistency. I can't know what future turnover will be, but I do remember writing in the past that it had become so consistent that whatever was behind it was likely to result in continued future turnover.

Since my most plausible (actually only) explanation was that the turnover was due to a pronounced physical tightness that is highly compatible with the continuing movement – because how can physical tightness in any commodity be ended with a continued lower price? Under the law of supply and demand, physical tightness or shortage can only be resolved by higher prices; if prices remain low, the tightness can't be alleviated. If the physical turnover in the COMEX silver warehouses is as a result of wholesale physical tightness (as I believe), lower prices should result in continued turnover, as would appear to

have been the case. This is one of those disconnects I referred to earlier.

Continuing with COMEX-related matters, the March silver delivery process is playing out with no big surprises, namely, JPMorgan is taking as much physical silver as it can for its own benefit without disturbing the price. In its house or proprietary trading account, JPM has stopped 781 contracts out of the 1049 total silver deliveries made so far this month. Without getting into unnecessary detail, JPMorgan has taken an even greater percentage of silver deliveries than the raw numbers suggest and with 350 contracts still effectively open in the March contract, it looks like the bank will pick up more than 1000 contracts (5 million oz) by delivery month's end. There is no doubt in my mind that if JPM could take ten or hundred times that amount of physical silver, it would do so in a heartbeat, so great is its appetite for physical silver.

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

Before switching over to ETF developments, I should mention yesterday's unusual increase of 500 contracts in the COMEX March gold futures contract. Most likely, but not certainly, the transaction was the result of a single buyer desiring physical delivery of 50,000 oz of gold before month's end. In terms of

ounces, this quantity of gold is not particularly noteworthy (certainly compared with the ETF flows), but it still represents $62 million, not exactly chump change for a single transaction. There is not enough specific data surrounding the transaction to speak in definitive terms, apart from it being somewhat out of the usual in dollar size and timing. But I can't help but make a point related to silver.

(Please note this represents a correction from the original article posted. In the original I misstated the dollar amount of the gold transaction as $625 million and everything that followed was off by a decimal point. What follows is the corrected version)

I just finished describing how JPMorgan seemed to be threading the needle, in trying to take as much physical silver as it could in the March futures contract without driving prices higher and it looked like they would be able to slightly exceed the 5 million oz mark. What I didn't say was how much that silver represented in terms of dollars, so let me do so now – about $80 million. Now compare that with the dollar amount of gold transacted yesterday. Stated differently, if a single buyer with $62 million to spend bought COMEX silver futures contracts for immediate delivery, instead of COMEX gold futures contracts, the number of silver contracts purchased would come to 800

COMEX contracts, or 4 million oz of silver.

I would submit that it would be quite easy to imagine a buyer with $62 million to spend buying silver instead of gold heck, I'd do so in a heartbeat, as I'm sure would many of you (if we had that much money to invest). The problem is that it couldn't be done because there isn't that much silver readily available. The absolute master of the financial universe, JPMorgan, is tweaking every leveler it can to pick up 5 million oz this month on the COMEX and there is no way anyone could place a buy order for 4 million oz of silver this late in the delivery process as just occurred in COMEX gold (maybe by JPM itself). That's just another way of saying there is not enough silver available for purchase compared to gold and that silver's price is disconnected from reality to an absurd degree.

While I contend that the main price driver for gold and silver is COMEX futures positioning, that is not to say that once prices are driven higher or lower, there are not related consequences. This week's sudden price surge to the upside in COMEX gold and silver did directly result in price-momentum type buying in the big gold and silver ETFs, GLD and SLV. As a result of Wednesday's late price surge, massive buying occurred in GLD that day and even more so in SLV on Thursday. As a further result of the net new buying that occurred in both hard

metal ETFs, it was simple to conclude that big actual metal deposits should be forthcoming. Over the past two days, some 765,000 oz of gold, worth close to $1 billion, have been deposited into GLD, as a result of Wednesday's buying. By my back-of-the-envelope calculations, that is roughly the amount I would have assumed were “owed” to the trust. Trading volume in GLD subsided to normal levels on Thursday and Friday.

My calculations are a bit different for silver. Wednesday's higher than normal volume, plus Thursday's super-high volume, caused me to calculate more than 6 million oz were “owed” to SLV, so yesterday's deposit of nearly 2.7 million ounces still leaves us more than three million oz shy. Complicating matters is that the cutoff for the next short interest report on stocks was Wednesday, meaning that any big short selling in SLV on Thursday will not be in next week's report. Somehow, I don't think that was accidental.

I apologize for my repetition, but I must point out that nearly one billion dollars' worth of gold was deposited into the GLD these past two day. If someone bought one billion dollars' worth of silver instead of or in addition to what was purchased in GLD that would amount to more than 60 million ounces of silver. I won't beat this to death, but please try to contemplate what would likely happen to the price of silver should anyone try to buy 60 million ounces in a

day.

There's not much new to report as far as Silver and Gold Eagle sales from the US Mint except a continuation of Silver Eagle sellouts and a cooling off in demand for Gold Eagles for reasons I previously discussed. So far this month, 23,000 oz of Gold Eagle have been sold, worth just under $29 million. For Silver Eagles, 2.26 million oz have been sold worth upwards of $38 million so far this month, or substantially more than the dollar amount spent of Gold Eagles. I know that these numbers change, but above I've made the point a number of times about what would happen if what was being spent on gold in terms of the COMEX and the ETFs was spent on silver. Just to demonstrate that that wasn't some unrealistic figment of my imagination, that is exactly what has transpired in US Mint transactions this month and Silver Eagles are being rationed to boot, which means even more Silver Eagles would have been sold if the Mint was able to keep up with demand.

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 largely as expected and immediately outdated as a result of the price surge after the

Tuesday cutoff for yesterday's report. Trading activity in the just reported trading week was choppy with a slight downside bias and I thought that what little change that was reported would be in the direction of a reduction in the total commercial net short position in both gold and silver. It largely turned out that way, but there was a surprise of sorts in gold.

In COMEX gold futures, the total commercial net short position was reduced by 9800 contracts to 185,500 contracts. The surprise was in the commercial category breakdown. The four largest shorts added 5400 new short contracts and the largest 5 thru 8 largest traders added a whopping 7500 new short contracts. The raptors (the smaller commercials apart from the big 8) went the other way completely, in buying back 22,700 short contracts. Given the wide disparity of behavior among the commercials, I first thought there might be a reporting error.

While that's possible of course, I'm more inclined to think that this might help explain the recent erratic and volatile trading patterns in gold. Gold has been "hot" this year and all markets that turn very active, tend to attract hot trading money. We've seen huge volumes of trading on the COMEX and equally huge changes in total open interest on an almost daily basis. What's happening seems to be aggressive and active trading between the commercials and big

speculators in COMEX gold, in addition to the usual commercial/managed money positioning tango? But it would be too soon to abandon the analysis of that traditional positioning tango.

There's still only one potential negative in gold and silver and that negative is the market structure on the COMEX. The COT approach may get blown out of the water, but it is too soon to conclude that. I'd be lying if I told you I was unconcerned that the biggest gold shorts on the COMEX now hold their largest concentrated short position in more than a year. I have to be consistent and just a couple of months ago, I was touting how bullish it was (and turned out to be) that the big COMEX gold shorts held low short positions.

I'm going to skip over changes on the managed money side of gold, except to note that with under 30,000 contracts held short, there still isn't much potential buying power from that quarter.

Likewise, there wasn't much to report in COMEX silver futures, as the total commercial net short position was reduced by 800 contracts to 70,000 contracts, about as small a change as typically seen. The big 4 bought back 400

short contracts and I'd still peg JPMorgan as being short 21,000 contracts. As was the case in gold, managed money short positions are now so low in silver (under 8,000 contracts) that no meaningful short covering appears reasonable.

Based upon trading volume, price action and daily changes in total open interest, if the new COT report was calculated as of yesterday, there would appear to have been a decently large increase in commercial selling, perhaps on the order of at least 15,000 contracts in gold and 7,000 or so in silver. That would put us at new bearish extremes in the COMEX market structure. Even though it is virtually the only bearish factor in place, it is not a minor factor.

Much continues to be written about the COT report situation in gold and silver, ranging from the structure guarantees a sharp price decline to the commercials being overrun and prices exploding. I even read one report saying that the COTs no longer matter at all. I'd label that as opinions running the full gamut. To my mind, the COT market structure is more important than ever, even though I can't profess to be certain of how this plays out. In a very important sense, a failure of the current bearish structure to resolve itself to the downside, as the probabilities suggest, would likely demonstrate just how significant this whole line of analysis is.

If anything was to cause the COMEX market structure to “fail” it would most likely be due to the forces of the physical market overcoming the decades' old price manipulation. Theoretically, this can happen in either gold and silver (or both), but as I tried to indicate above, given the amount of money it would take in silver versus gold, the safe bet is that it would happen more in silver.

And while it does appear to me that the probabilities for a price unwinding to the downside still hold the upper hand, there is one specific factor in silver that makes me as nervous as a long-tailed cat in a room full of rocking chairs. The fact that I am convinced beyond doubt that JPMorgan has acquired 400 to 500 million ounces of physical silver means that no matter what happens, JPMorgan is set to make the financial score of the ages when silver explodes in price. Yes, I still believe they will likely succeed in buying back tens of millions of ounces of their COMEX short position on lower prices, but for the first time in history, this bank owns enough physical metal to make that short covering less necessary.

One final word. The price of gold and silver have been higher for long enough (7 weeks) that the important 50 day moving average is now rising sharply on a daily basis. In a matter of a couple of weeks more, the 50 day moving average

in gold will be well over the $1200 mark and silver well over the $15.20 level. That's just the mathematical consequence of moving averages. Perhaps the commercials have waited to press the technical funds until the stop points to the downside haven't been so far away. I guess I still lean to the probabilities of eventual technical fund selling on lower prices, but should a silver physical shortage kick in (with any decent dollar amount of investment buying) while the commercials are so exposed and vulnerable on the short side, the COTs will matter more than ever before.

Ted Butler

March 19, 2016

Silver – $15.80 (50 day moving average – $14.89)