Weekly Review

Following nearly two months of a protracted (and orchestrated) price swoon, the price of gold and, especially, silver rose this week. After ending the previous week at the lowest levels of this year and close to the lows of the past five years, gold added $24 (2.1%), while silver surged by $1.09 (7%). As a result of the strong relative outperformance of silver compared to gold, the silver/gold price ratio tightened in by more than 3 full points to under 71 to 1. The ratio is still within the broad trading range of the past six months, but now sits at the lowest levels of the range and threatens to move much lower (silver outperforming).

It's no secret that I favor silver over gold for a variety of reasons, including relative availability, silver's utility value and the puny amount of investment money needed to impact the price of silver. That said, there has been something about the relative price change in the ratio in 2015 that I've been thinking about but not writing about. After slightly outperforming gold on the price rally from the end of December the end of January (but not by much), silver has performed much better relative to gold than usual on the price decline from the end of January to last week.

At the extremes, gold fell $160 from the January highs to the recent lows, while silver fell $3. On a gold price decline of that magnitude, I would have expected a much bigger price beating in silver. I have been thinking a lot about that recently and there are a number of explanations that come to mind, mostly centered on how utterly stupid cheap silver had become, both in absolute terms and relative to gold and most other commodities. In other words, maybe silver didn't decline as much as it usually does when gold declines because it was already stupid cheap.

I suppose the longer the price of anything stays ultra-depressed regardless of the cause, the less extreme that depressed price may appear. But appearance is one thing and just because our senses become dulled from experiencing a long bout of an extremely depressed price, doesn't mean the price isn't extremely depressed and likely to readjust upward dramatically. And as the relative price action suggested this week, we may be at point where silver may truly accelerate to the upside, both in flat price and relative to gold. As I hope I have conveyed, based upon market structure (COT) considerations, the bottom in silver and gold was in sight as the last technical fund short was established. The more important question was, therefore, what would the ensuing rally look like? More on that in a moment.

A large physical withdrawal on Friday increased the weekly turnover or movement of metal into and out from the COMEX-approved silver warehouses to nearly 3.9 million oz, as total inventories fell 1.4 million oz to 174.9 million oz. While still below the weekly average of the past year (5 million oz), this week's movement is the annual equivalent of 200 million oz, not exactly chopped liver. There has been a pickup in the movement of metal in the COMEX gold warehouses, including the new category of gold in kilo bar form on the COMEX, which also indicated unusual turnover on Friday.
http://www.cmegroup.com/trading/energy/nymex-delivery-notices.html

I'm still of the opinion that the physical movement in the COMEX silver warehouses is more meaningful than the movement in COMEX gold warehouses when I step back for a more prospective view. That's because the quantities of metal involved relative to how much of each exists in the world are miles apart. In silver, the total level of metal in the COMEX warehouses (175 million oz) and the annual turnover (more than 200 million oz) come close to being 20% of the one billion oz of silver bullion in the world. In gold, the COMEX inventories (including the new kilo category) amount to less than 9 million oz or less than half of one percent of the 3 billion oz of gold bullion in the world (of the 5.5 billion total gold oz in all forms).

Stated differently, it seems more reasonable to me to study an inventory that makes up 20% of total world inventory for clues, than in studying an inventory that comprises 0.3% of total world inventory. That's why I don't dwell on the COMEX gold warehouses that closely; it would be like studying just one or a few oil or grain storage facilities and trying to gauge total world inventories. COMEX silver inventories are a much bigger subset of total world silver inventories and may yield important clues because they are such a big sample. That's not the case in COMEX gold inventories and this necessarily makes analysis more speculative. Now, if we're talking about COMEX gold (and silver) futures positioning and the impact on price, then the COMEX is number one. But COMEX gold paper (electronic) trading and warehouse inventories are different things and should be viewed that way.

I am going to gloss over changes in sales of Silver Eagles or in the big silver ETF, SLV, since I mentioned each on Wednesday. Certainly, given the late week price action, any future changes should prove instructive. The same goes for JPMorgan stopping (taking) deliveries against the COMEX March silver futures contract in its house or proprietary trading account. The bank continues to take the lion's share of deliveries (1153 out of the total 2043 issued), but deliveries, which are at the sellers' option of deciding when they will be issued, are dragging a bit. Based upon the remaining open interest in the March contract, JPM still looks in line to receive 200 to 300 more deliveries before month end. http://www.cmegroup.com/delivery_reports/MetalsIssuesAndStopsYTDReport.pdf

The changes in this week's Commitments of Traders Report (COT) met and exceeded expectations, particularly in gold. Given that silver and gold prices were somewhat lower during the reporting week ended Tuesday and, more importantly, were being sliced, salami-like, to new lows extending back some time meant there would undoubtedly be reductions in the headline number of the total commercial net short positions in COMEX gold and silver. Those reductions were duly reported yesterday.

The key open question was if the very last technical fund short position had been placed in COMEX gold and silver, meaning that the price bottom was put in, at least temporarily. I strongly suspected that we were very close to that point, but wrote that one could only know with certainty after the fact. The key open question has now been answered definitively by the price rally since the Tuesday cutoff. Because it's certain that the price rally that started late Wednesday afternoon was primarily fueled by technical fund short covering in COMEX gold and silver that means it is also certain that we have passed the extreme peak in technical fund short sales. Now only one question remains the extent of the rally.

In COMEX gold futures, the headline total commercial net short position decreased by another whopping amount – 32,800 contracts, to 56,500 contracts. (I had guessed a reduction of 10,000 to 15,000 contracts and am very happy it was a lot more). That means the total commercial short position is down by a remarkable 150,000 contracts (15 million oz) from the late January highs.

Please think about that for a moment. Technical funds and other speculators have sold and sold short 15 million oz of electronic gold on the COMEX (which the commercials arranged and prearranged to buy) on the $160 decline in price. This is either a coincidence (which recurs continuously) or the cause of the price decline. It's gotten to the point where I feel sorry for those who refuse to see the obvious.

By commercial category in gold, it was a big 5 thru 8 and raptor affair, as the big 4 actually added close to 900 new short contracts. The big 5 thru 8 bought back 10,000 short contracts and the gold raptors added 21,700 contracts to a net long position now amounting to 75,400 contracts. This is the largest (most bullish) raptor long position since the gold price bottom of last November and among the largest raptor long gold positions on record. Likewise, the total commercial net short position is the lowest (most bullish) position since last November and in history.

If anything, the counterparty selling by the technical funds was even more impressive. Traders in the managed money category of the disaggregated COT report sold more than 29,000 contracts, including a further long liquidation of more than 9000 contracts and new short sales of more than 20,000 contracts. That puts the managed money long position close to the previous low and makes it unlikely for there to be significant further liquidation and downward price pressure. It also puts the managed money short position near record extremes and means not only no further selling but also represents a full tank of rocket buying fuel to the upside. Simply put, these are beautiful numbers if one is bullishly inclined on gold. The managed money net long position (longs minus shorts) is now the lowest (most bullish) since the end of 2013. When this year began (and into January) I never thought the commercials could arrange to get the technical funds configured like this in gold; but they have.

In COMEX silver futures, the total commercial net short position decreased by

3100 contracts to 30,200 contracts. (I had guessed a reduction of 3000 to 5000 contracts on Wednesday). This is the lowest (most bullish) headline number since the beginning of December and is more than 30,000 contracts (150 million oz) lower than the peak short position of late January. As was the case in gold, the sale of 150 million oz of electronic silver contracts on the COMEX by the technical funds and other speculators is the sole explanation for the $3 drop in price at the recent lows.

By commercial category, the Big 4 bought back around 1000 short contracts, while the big 5 thru 8 added 2200 new shorts (the opposite of what occurred in gold). Somewhat surprisingly, the raptors added 4300 new longs to a net long position now totaling 28,400 contracts, the most since late November. I'd peg JPMorgan's short position at 13,000 contracts, meaning the bank is not the largest short in COMEX silver. There have not been many occasions over the past seven years where that has been the case.

As was the case in gold, the counterparty selling by the technical funds in silver was even more remarkable than the commercial buying. Traders in the managed money category added more than 5000 new short contracts, increasing the technical fund short position to 31,500 contracts. At this point, it is safe to say that will be the peak in technical fund short sales for some time.

Interestingly, managed money longs increased by a thousand contracts to 43,000 contracts, reinforcing my premise of a core 40,000 contract long position not likely to be liquidated on lower prices.

Since the key question of when and at what price the last technical fund short contract would be established in COMEX gold and silver has been answered by the late week rally, all that matters now is the extent and nature of the rally that has commenced. From past experience, we also know what will determine the extent and nature of the rally, namely, the degree of aggression in the commercial selling which must occur when the technical funds buy. Will that commercial selling be as aggressive on this rally as it has been on recent rallies over the past couple of years? As time has progressed, the rallies in gold haven't amounted to much more than a hundred dollars or so and silver rallies haven't exceeded $3 for some time.

Moreover, we also know from experience that within the commercial community, when the raptors in COMEX gold and silver are as heavily long as they were on the cutoff, these traders are most likely to be the early commercials on the sell side, taking quick profits from technical fund shorts which buy as prices climb. Usually, the big 4 and 8 in COMEX gold and silver don't add to short positions until much of the raptors long liquidation has occurred. These big commercial shorts, led by JPMorgan in silver have become the de facto short sellers of last resort because without the price capping that the increase in concentrated short selling represents, silver prices, in particular, would run away to the upside. That's why it's easy for me to label JPMorgan as the big silver manipulator and crook without fear of consequence.

Upfront, please don't take what I am about to write as what will happen on this embryonic silver and gold rally because no one can tell you what will happen price wise with certainty (even though the COT analysis has been so accurate recently as to be unnerving). I know what should happen (at least in silver) and maybe outline what is likely to happen; but there's a difference between prophecy and analysis, so please take it in that manner.

There's no doubt significant technical fund short covering has occurred in gold and silver over the past two trading days, although how much is hard to say. After trading below key moving averages for the better part of the past six weeks, in two days we penetrated several important moving averages in silver to the upside on a closing basis, including the 20 day (and all shorter) moving averages, the 30 day and 40 day and even the 100 day moving average. Prices penetrated the key 50 day moving average on Friday and closed right on it. Just like the technical funds respond to downside penetrations in the moving averages by selling and selling short, they respond to upside penetrations by covering short positions and going long. Once again, this is the essence of the market.

What's most remarkable about the price action over the past two days in silver is that the speed and force of the two and a half day rally does not appear to be in keeping with the four previous anemic $3 silver rallies dating back to the beginning of last year. Plus, as I mentioned earlier, silver has acted funny over the past six or seven weeks in that it was not as relatively weak compared to gold on the downside as it had been in the past.

I know I warn against relying on price action in a manipulated market, but there's something different this time silver wasn't as weak as it usually has been and is out of the gate quicker and stronger than it has been recently as well. To that I would add the masterful work of art, worthy of Picasso himself that the commercials rigged in getting the technical funds as short as they were in the current COT, to say nothing of JPMorgan's accumulation of a massive amount of physical silver.

I suppose it's possible for the commercials to slam on the price brakes at any time, but usually there is a cycle and season to price capping that evolves over time periods longer than a few days or weeks. And in order to lure the technical funds back onto the short side the commercials would have to rig a sudden and violent drop in the price of silver below recent lows and even if the commercials did rig such a price drop (this is still a manipulated market after all), it probably wouldn't lure near enough technical funds back to the short side as existed as of Tuesday. The technical funds are much more comfortable in building big short positions on salami slicing-like price declines, rather than on big chunks to the downside.

For a variety of reasons, including expecting it for many years, I'm inclined to view this budding rally in silver as the big one. In any event, that's how I plan to handle it, namely, with little thought given to selling in the near term, no matter how far the rally may extend, including speculative call option positions. I will only get defensive (as I was around the end of January) as and when the no good rotten commercial crooks on the COMEX dramatically increase their manipulative concentrated short position as the rally continues.

While there is no question that the last technical fund short position was in place as of the Tuesday cutoff and that there has been significant technical fund buying in the form of short covering (and maybe some new buying), I'm guessing that the raptors have been the big sellers over that past couple of days, as is their custom. I'm also inclined to believe that the big commercial shorts, particularly JPMorgan, have not added significant new short positions to cap the price. I'm hoping the speed and force of the two and a half day silver rally was directly related to the absence of manipulative short selling by the big commercials.

The beautiful thing is that we'll know soon enough both in price action and future COT data. While the raptors have (or had) a large long position that can and will be sold as silver and gold prices rally, raptor long liquidation is rarely enough to cap prices by itself. New and aggressive short selling by the COMEX's largest commercials has always been needed to cap price rallies and absorb total technical fund short covering and new long positioning. That same equation exists today, but what has changed is that the price of silver has been in the stupid cheap category for too long and JPMorgan is fully positioned on the long side of physical silver. A sharp upside move in silver, therefore, won't hurt and will, in fact, benefit JPM immensely.

I can't rule out this developing silver rally petering out in the manner of the rallies over the past couple of years (with JPMorgan singlehandedly capping the price), but neither can I rule out a major price move uptown. At this point, there still appears to be great skepticism about the rally so far, but no real COT advocate would feel that way. Or, at least this advocate isn't skeptical. Someday, this silver price manipulation will end and it will then be obvious to all just how stupid cheap the price had become. Of course, the big money will be made by those who recognize this before it occurs.

Ted Butler

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Silver – $16.73

Gold – $1182