A Friday selloff pushed gold lower for the week by $6 (0.5%) and its lowest close in 3 months. Silver, also down sharply on Friday, managed to finish unchanged for the week, thanks to the sharp rally on Wednesday. As a result of silver's slight relative outperformance, the silver/gold price ratio tightened in by a fraction of a point to 75.4 to 1. Not much to see here.

Regarding the sharp jump in silver prices midweek and the subsequent Friday selloff, the preponderance of the evidence points to "scam within the scam" type positioning in COMEX futures as being the cause. Suspicions of this were seemingly confirmed with yesterday's release of the weekly Commitments of Traders (COT) Report. I'll get into the details in a bit.

The turnover or physical movement of metal brought into or removed from the COMEX-approved silver warehouses amounted to 4.9 million oz this week, close to the weekly average over the past 6.5 years, or an astounding annual rate of 250 million oz. It was another decidedly "in" week, as total COMEX inventories rose by 2.5 million oz to 227.1 million oz, another multi-decade high. Conforming to the recent pattern, there was nothing turned over in the JPMorgan COMEX silver warehouse, which stood at 115.8 million oz.

I would note that over the past year, total COMEX silver warehouse inventories have risen by 50 million oz, with around 35 million oz of that having been deposited in the JPM warehouse. While a 30% increase (or decrease) in any exchanges' total approved physical inventories is not exactly small potatoes, it is hardly unprecedented. What is highly unusual and unprecedented is the physical turnover in COMEX silver inventories, something never witnessed in any other commodity.

The real intrigue is not the 50 million oz increase in COMEX silver inventories over the past year, but the 250 million oz physical movement last year and every year for the past five and a half years before that. Since the information is reported daily (for free) and widely followed, I remain thunderstruck by why so few ever comment on it. I'm not declaring that my explanation for the unprecedented COMEX silver inventory turnover is correct (although I think it is), I'm just genuinely perplexed the verifiable turnover is not the focus of more attention.

My explanation is that the extreme physical turnover is caused by underlying supply tightness and has served as one of JPMorgan's prime means of acquisition for physical silver over the past 6.5 years. I contend that the frantic physical turnover enabled JPM to "skim" 100 to 200 million oz off the turnover accounting for big part of its total silver hoard (650 million oz). You'll remember, of course, that the unprecedented turnover began in April 2011, the exact moment JPMorgan decided to begin to accumulate physical silver and open its own COMEX warehouse. In the time since, I've asked and continue to ask for alternative explanations for the unprecedented physical silver turnover.

I'm going to skip over COMEX deliveries, ETF deposits/withdrawals and Silver and Gold Eagle sales from the US Mint (which still stink) and, in any event, hold no strong influence on gold or silver price levels or changes. Let me jump to the changes in this week's COT report. As a reminder, I ventured no predictions given the relatively subdued price action, although the salami slicing price action of the reporting week was explained by managed money behavior in silver and also explained the sharp rally on Wednesday.

In COMEX gold futures, there was almost literally no change in the total commercial net short position which stayed at 210,700 contracts, a somewhat rare occurrence. This week marked the fifth or sixth straight week of relatively minor positioning changes in gold or silver and concurrent minor price changes, which reaffirms what causes price change. With no change in the commercial headline number, big changes by commercial category were highly unlikely. The big 4 added 700 shorts, the raptors sold off 200 longs and the big 5 thru 8 bought back 900 short contracts. Nothing much to see here, except that the positioning resolution still lies ahead.

On the managed money side of the COMEX gold ledger, these traders sold 2403 net contracts, including the sale and liquidation of 10,049 long contracts and the buyback of 7646 short contracts. The short covering was more surprising than the long liquidation and with only 16,687 short contracts remaining, further big managed money short covering would appear near impossible. The key question remains if the managed money traders can be induced onto the short side in great numbers in gold, but particularly in silver. Time will tell.

Friday's close left gold less than $10 above its important 200 day moving average, which if penetrated to the downside has usually served as inducement enough for managed money selling, both of the long liquidation and new shorting varieties.

In COMEX silver futures, the commercials reduced their total net short position by 5500 contracts, the biggest weekly change in five weeks. Still, the market structure hasn't changed much over the past nearly two months and neither has price. By commercial category, all three groups were on the buy side, but the raptors (the smaller commercials) lived up to their reputation for being quicker to the kill in adding 4600 new longs (now up to 27,800 contracts net long), while the big 4 bought back 400 short contracts and the big 5 thru 8 bought back 500 short contracts. I'd peg JPMorgan's short position to be 36,000 net contracts, down 500 for the reporting week. Next week's Bank Participation Report will allow further calibration.

On the sell side of COMEX silver futures, the managed money traders sold 6605 net contracts, including the sale and liquidation of 1808 long contracts and the new short sale of 4797 contracts. The increase in managed money shorting was interesting for two reasons. While not large at 15,357 total contracts held short, the increase this week might suggest there is more such new shorting on new price lows ahead. The other thing is that this week's increase in managed money shorting was likely the catalyst and target behind the sharp price rally on Wednesday.

Having just positioned the managed money traders onto the short side through Tuesday's close, what better way for the raptors to cash in on their just-added long positions than by inducing managed money short covering on the Wednesday rally, which popped up to the two key silver moving averages? In Wednesday's report, I couldn't be sure what the price jump that day was all about, but with the subsequent price action and new COT report, it certainly appears the price changes were of the scam within a scam variety or a dipsy-doodle move.

What's interesting in these short term positioning moves is that they are generally of the raptor vs the managed money traders and not so much the big 4 or big 8 positioned against the managed money traders. The biggest commercials seem more interested or capable in larger price moves and positioning changes, rather than in scooping up every last nickel and dime on a short term basis. One way to see this is in the overall money scoreboard running tally.

I would estimate that the short term pop in silver prices on Wednesday and subsequent smash yesterday involved roughly 5000 net contracts or so and around

30 or 40 cents per contract that the raptors made and the managed money traders lost. Thus, I would quantify the silver raptors' gain and the managed money traders' loss to be around $7.5 to $10 million, not an insignificant amount for a very short term trade to be divided between the dozen or so traders involved.

However, to achieve that realized short term positioning and gain/loss, the overall mark to market experience of the 8 largest shorts in silver had to move much more. A forty cent pop in the price of silver equates to a $200 million adverse money move for the 8 big shorts, a much more significant amount than the $7.5 to $10 million made and lost by the raptors/managed money traders. Like a ten ring circus, there are different levels of activity and traders involved in COMEX silver and gold. The trick is trying to identify and quantify what's going on in the most important circus rings – sometimes the elephant parade takes center stage, other times it's the clowns.

Despite the mid-week excitement in silver in which total open losses grew as much as several hundred millions of dollars at the price peaks, by week's end the 8 big COMEX shorts broke even on silver and were ahead by $150 million in gold in terms of unrealized gains/losses. That puts the 8 big shorts combined position in the black by $150 million (after being in the red by as much as $2.7 billion three months ago). If there is a more cogent and accurate explanation for what is moving both short term and long term prices in gold and silver away from COMEX futures contract positioning, that reason continues to elude me.

As for what transpires from here, it still looks like the probabilities favor a downside price resolution featuring managed money selling and commercial buying on lower prices. But that is far from guaranteed, even if that has been the very reliable pattern of the past. I wish we would get to whatever resolution lies ahead quickly, but I wish for a lot of things; only some of which come true.

Bitcoin and the CME Group

This week, Bitcoin prices surged to new highs and one big reason was said to be the announcement from the CME Group, Inc. that it intended to introduce a Bitcoin futures contract by yearend. Before I get to the CME announcement, a few words on Bitcoin, which I've tried to avoid, largely so as not to appear like an expert in all things financial, an appearance apparently sought by many others.

But it's hard not to notice the incredible price rise in Bitcoin and other crypto-currencies over the past decade or less and the subsequent total market capitalization, said to exceed $100 billion and even $200 billion. That's more than ten times the market capitalization of silver in the form of 1000 oz bars and silver had a head start of several thousand years.

I'm not computer oriented in the slightest, so I freely admit to having my eyes glaze over with technical talk about the mechanics of Bitcoin and the block chain, the technology that enables it. As a result I've never bought Bitcoin and unless hell freezes over or some other such equivalent event occurs (like me becoming a computer expert), I will end up missing whatever is to come in that realm, both good and bad.

My sense is that the vast majority of those buying or likely to buy Bitcoin or other crypt-currencies are not enamored with its technology so much, but are motivated strictly by the fact that it has risen so much in price, from pennies to more than $7000 per Bitcoin. Some things I learned early on (decades ago) were that there is no limit as to how high a stock or commodity or any other investment/speculative asset could rise and that once investment manias take hold, there is no telling how far they may carry, although such manias always seem to crash and burn at some point.

I would define a speculative mania as one in which collective new buying is the sole driver of price. In this sense, Bitcoin appears no different than past manias, except that it is much bigger and international in scope and has more new participants than any previous manias I'm familiar with. In all past manias, the collective new buying that drives prices much higher than expected, eventually turns into collective selling and prices collapse. While I have no dog in this fight and wish everyone well, sooner or later, that which soars on collective buying, must crash on collective selling.

The one strong (and encouraging) lesson I take from the Bitcoin experience to date is the reaffirmation that investment crowds tend to be mad, throwing all caution to the wind on the buy side as prices continue to rise, only to revert to panic selling at some point. While I can't tell you when, I can tell you that there will be a great investment mania in silver one day. All you need for a mania is a great story line and a period of collective money inflow. Considering just how great the real silver story is and how little the amount of money is that it would take to launch it to the heavens, it is surely only a matter of time before the two meet.

But the impetus for today's comments on Bitcoin is not just the dramatic price increase of late, but the proposed role of the CME in introducing a futures contract on it. There is no question that the CME (owner-operator of the COMEX and other futures exchanges) senses the enormous profit-making opportunity that a brand new actively traded contract might bring and is rushing to be the first exchange offering trading in it. The keys to an actively traded futures contract are price volatility and widespread participation, both features apparent in Bitcoin. However, I'm torn by other considerations.

Admittedly, I tend to see things differently than others when it comes to futures trading, given my own personal and professional experiences. These are the experiences, some very painful, that have driven my interest in silver and, particularly, in my allegations of price manipulation emanating from COMEX positioning. Those personal experiences play a key role in my concern about the CME instituting a futures contract on Bitcoin.

Futures contract trading in the US exists because Congress has authorized such trading and has insisted that it be regulated by a federal agency, the Commodity Futures Trading Commission (CFTC). Neither Congress nor commodity law ever intended that regulated futures trading exist for the sole purpose of allowing a purely speculative trade, another gambling venue like Las Vegas. Instead, regulated futures trading was intended for the purpose of enabling legitimate producers and consumers of commodities to lay off the unintended price risk associated with the normal production and consumption of commodities, commonly known as bona fide hedging.

Speculators are needed so that legitimate hedgers can lay off the price risks they seek to avoid, but it was never intended that speculators would come to run the whole price show, as has developed in COMEX silver, for instance (where real producers and consumers have been excluded and only speculators remain). I don't know that there are any legitimate producers or consumers in Bitcoin or that even if there are any, they are looking to hedge unwanted price risks associated with Bitcoin production and consumption.

The CME's rush to introduce a futures contract on Bitcoin is about capturing the fees that would be generated by speculators on either side of the market, just like a decision to build a new casino on the strip in Vegas. The problem is that one has to come up with a pretty convoluted definition of legitimate hedging in order to use it as the economic justification for a Bitcoin futures contract. I'm sure this might prompt the CME to craft some plausibly sounding hedging justifications, but I've seen none to date, just the hope of capturing the potential enormous speculative trade. At least in silver, I suppose the legitimate producers and consumers could participate in COMEX trading if they wanted to; in Bitcoin, I don't see how such legitimate producers and consumers even exist.

Of course, the CFTC would have to approve any trading of Bitcoin as a futures contract, but the sad truth is that the agency is not much more than an extension of the will of the CME Group or JPMorgan. What Lola wants, Lola gets. Still, the next time you see that ubiquitous CME TV commercial which features Sir Richard Branson at the end picking up and pocketing a golf ball against the background of the CME existing for the purpose of allowing legitimate hedging, please think about legitimate hedging and Bitcoin.

Further, the last paragraph of the CFTC's mission statement and responsibilities is this –

"The futures and swaps markets are essential to our economy and the way that businesses and investors manage risk. Farmers, ranchers, producers, commercial companies, municipalities, pension funds, and others use these markets to lock in a price or a rate. This helps them focus on what they do best: innovating, producing goods and services for the economy, and creating jobs. The CFTC works to ensure these hedgers and other market participants can use markets with confidence."

http://www.cftc.gov/About/MissionResponsibilities/index.htm

When it comes to explaining and justifying futures trading, it's always about the ranchers and farmers and legitimate producers that everyone is supposedly trying to protect. But when it comes down to brass tacks and realty, it is only about enabling speculators and the few firms and exchanges that control trading and rake in the profits.

Ted Butler

November 4, 2017

Silver – $16.85 (200 day ma – $17.18, 50 day ma – $17.21)

Gold – $1270 (200 day ma – $1261, 50 day ma – $1300)