November 8, 2014 – Weekly Review

Weekly Review

In the largest one day rally in ages, the price of gold surged in late Friday trading to end up $5 (0.4%) for the week; this after falling to new 4+ year lows in pre-dawn trading. Silver also snapped back Friday after establishing new price lows in earlier overnight trading, but still finished down 40 cents (2.5%) and at the lowest weekly close in nearly five years.

As a result of silver's anemic relative price performance, the silver/gold price ratio blew out to more than 74.5 to 1, after trading even higher. Upon glancing at some charts, it looks like this is the highest price ratio and most extreme discount that silver has been at compared to gold since 2009. Since I repeat incessantly my conviction that silver will greatly outperform gold on a long term basis, that it has done the opposite for the past several years requires some explanation.

All the current facts, as I know them to be, continue to indicate silver is in greater relative demand, tighter relative supply and more undervalued to gold (and every other asset) than ever. I'll try to highlight those facts this week as I do every week, but those verifiable facts are being overshadowed by a COMEX price manipulation that has always been more pronounced in silver than it has been in gold or any other commodity. But all manipulations must come to an end and there are increasing signs pointing to the end of the historic silver manipulation. That end will not only light a fire under the price of silver, it will shock those who could have switched to silver from gold or any other asset but didn't.

My prime indicator of conditions in the wholesale silver market Â? turnover or movement of metal into and out from the COMEX-approved silver warehouses Â? continue to flash signs of tight supply. Inventory not in great demand tends to sit there; stuff in high demand gets turned over more frequently. By that measure, I don't know how physical silver turnover in the COMEX warehouses can get turned over more frequently than it has this year, averaging more than 4.5 million oz each week.

This week, more than 6.5 million oz either came in or were shipped out of the six COMEX silver warehouses, as total inventories slipped by 600,000 oz to 179.9 million oz, not far from inventories at year end. Annualized, this week's movement is the equivalent of almost 340 million oz or more than 40% of total world mine production. This has never occurred in any other commodity and, as such, one would think the phenomenon would at least draw some attention.

There has been a recent noticeable pick up in the turnover of metal in the COMEX-approved gold warehouses that bears monitoring and I'm hopeful that it might attract more attention to the unprecedented silver inventory movement. After all, the pickup in COMEX gold inventory movement has existed for a few weeks; in silver it has persisted for a few years. If the pickup in gold turnover indicates a developing tightness (as seems reasonable), it can only mean conditions in silver are that much tighter.

There still seems to be a disconnect between the relative holdings of metal in the leading metal Exchange Traded Funds (ETFs). While not declining at the rate of last year when 40% of the gold departed the big gold ETF, GLD; the reductions in gold ETF holdings continued this week. The amount of gold held in GLD has now slipped to levels not seen since 2008. In contrast, since 2008, metal holdings in the big silver ETF, SLV, have roughly doubled and have remained steady over the past few years. The price of silver is down substantially both on an absolute and relative to gold basis, yet appears to be held much stronger by investors than has been the case in gold. Other than price manipulation, I'm at a loss to explain how that could be, by looking at relative price performance.

This week, the US Mint announced that it had exhausted its inventory of Silver Eagles due to strong demand, but would continue producing 2014 coins. I doubt the Mint will produce many more Silver Eagles this year, given the time remaining and the requirement it retool and produce for new coins for 2015. As has been the case on many occasions over the past few years, the Mint has failed to keep up with demand for Silver Eagles, even though it is required to do so by law. As a reminder, the Mint has not run out of Gold Eagles over this time (save for a temporary shortage of one-tenth oz Gold Eagles). Since there are not enough Silver Eagles for the Mint to sell, sales for the remainder of the year will be necessarily restricted, so we will see a trail off in Silver Eagle sales.
http://www.usmint.gov/about_the_mint/index.cfm?action=PreciousMetals&type=bullion

I've always maintained that demand or lack thereof for Silver Eagles and other retail forms of silver are important on a longer term basis, but have little influence on the wholesale price of silver. Then again, at close to 5% of total annual mine production, the demand for Silver Eagles is not exactly chopped liver and needs to be analyzed. There are two things about the US Mint's announcement that blare out to me. One is personal but hopefully not trivial; the other is potentially much more substantive.

I've been writing for quite some time that I sensed the presence of a big buyer in Silver Eagles and that the strong sales over the past few months and past few years have come when retail demand has been lacking. By process of elimination, the strong demand, if it wasn't coming from the retail public, had to come from a more concentrated source. Further, I speculated that JPMorgan was the Mr. Big behind the extraordinary buying of Silver Eagles. I even alleged that JPMorgan, since it knew silver prices were about to collapse in mid-summer (because it would cause prices to collapse), suddenly stopped buying Silver Eagles for three months, which created an inventory of unsold coins at the Mint.

In the October 4 Weekly Review, I laid out the case for why I thought there was a Mr. Big buying Silver Eagles and why I speculated it was JPMorgan. In the next weekly review (Oct 11) I had calculated that there may have been 4 to 5 million Silver Eagles in the US Mint's inventories and that JPM had purchased 3 million (after it resumed purchases), leaving only 1 to 2 million coins in inventory. The Mint's announcement dovetails perfectly on an amount and timeline measure to my comments. The Mint's announcement proves there was a fairly sizable inventory which didn't exist prior to JPMorgan's stepping away in summer; and when the sales resumed they resumed stronger than ever and again with no obvious retail demand. I wrote that JPM played the Mint (and US taxpayers) like a fiddle in letting the Mint build up inventory that Mr. Big would soon take off THE Mint's hands, but only at much lower (and manipulated) prices. Hey, we're talking about JPMorgan and that's the way these boyz roll.

Maybe I'm delusional, but I see the Mint's announcement as confirmation of my previous analysis. I don't think the Mint has ever held an inventory of Silver Eagles worth mentioning since April 2011 when I am convinced that JPMorgan embarked on a determined campaign to acquire as much physical silver as it could and in any form available. That aside, there's a hidden message also blaring out to me that silver investors should appreciate.

I think that what has just transpired with Silver Eagles from the US Mint is analogous with silver inventories and availability in all forms of silver, particularly including industry standard 1000 oz bars. This is the form of silver that will determine silver prices and any genuine silver shortage. The lesson from the Mint is that while the supply of silver may appear plentiful and widely available, the supply lines are not deep and very fragile. This is something I've noticed for many years, namely, even in times of apparent over supply, the supply never gets burdensome. In fact, silver is never really over supplied, rather there are times in which it is under demanded.
But unlike available supply, silver demand can erupt in a New York minute.

Thin supply lines are almost unique to silver, given the incredibly tiny amount of total silver bullion in the world, especially in dollar value terms, and silver's unique role as an industrial commodity and investment asset. In a very real sense, since most above ground silver is held by investors, world inventories are not actually working inventories, but investment holdings. Because they are primarily investment holdings, world silver inventories will only be available when existing investors decide the price is high enough. Same for gold, except with 300 times more gold in the world than silver (in dollar terms), gold supply lines could never be considered thin when compared to silver. A few months ago, no one thought the US Mint would run out of the highest inventories it ever held of Silver Eagles, yet that is clearly the case. The same structure of supply exists for 1000 oz bars Â? there's plenty until demand increases. Further, the frantic turnover of 1000 oz bars in the COMEX silver warehouses indicates thin wholesale supply lines.

The changes in this week's Commitments of Traders (COT) and monthly Bank Participation Report were instructive and in the case of gold, quite dramatic, if not mostly expected. I was off quite a bit in my expectations for technical fund activity in silver, but there was nothing alarming in the numbers upon further review. During this reporting week (ended Tuesday), silver fell more than one dollar and fell to new four year lows, while gold did the same in falling more than $50.

In COMEX gold futures, the commercials reduced their total net short position by an astounding 43,600 contracts, to 55,300 contracts. This is the lowest (most bullish) total commercial net short position in a year and among the lowest COT readings over the past decade. I had been expecting the commercials to undo the more than 40,000 contracts they had net sold on the recent two week rally that touched the 50 day moving average in last week's and this week's reports, but the commercials bought 10,000 more contracts than I guessed.

Let me just stop for a moment to restate the obvious. The reporting week featured a sharp decline in the price of gold in which important new lows were established. And just as has been the case on every important price decline in gold (and silver) throughout history, the commercials were the big buyers and the technical funds and other speculators were the big sellers. That's why I guessed the commercials had purchased close to 40,000 gold contracts over the past two reporting weeks. The fact that there has rarely, if ever, been an exception to this pattern proves the price manipulation on its face. There is nothing in terms of the free market that could begin to explain the regularity of price moves and positioning on the COMEX; the only explanation leads to manipulation.

All three commercial categories joined in on the buy side as is also usually the case on big moves. The big 4 shorts and big 5 thru 8 bought back 11,000 gold contracts combined with the raptors buying a chunky 32,000+ gold contracts. Based upon a big jump in the holdings of the 4 largest gold longs (not shorts), I was all set to report that JPMorgan had beefed up its net long position in gold, until I cross-checked the Bank Participation report. It wouldn't appear mathematically possible that JPMorgan could hold much more than 20,000 contracts net long. Combined with what I'll discuss in a moment in silver, I get the distinct impression that JPMorgan may be moving away from the COMEX. We'll know for sure when the lopsided structure in COMEX gold and silver gets resolved.

On the sell side of COMEX gold futures during the reporting week, the technical funds accounted for almost half of the contracts sold and I was surprised it wasn't more. The technical funds (in the managed money category) did sell a total of more than 21,000 gold contracts, but only a bit more than 6000 contracts were new short sales. While not the record above 80,000 contracts that I hoped for, at more than 74,500 contracts held short in the managed money category there is nearly a full load of rocket fuel in the tank.

What stood out in this week's report for gold (and silver) was the behavior of the other reportable traders and the non-reporting traders. Basically, the key difference between these two categories is that the other reportable traders hold positions in gold of 200 contracts or more (150 contracts in silver), while the non-reporting traders hold positions less than that. This week, the other reporting traders combined with the non-reporting traders sold more than 22,000 net gold contracts, including more than 20,000 new short contracts, an absolutely stunning amount. In fact, the non-reporting traders are more net short in gold than at any time in 15 years.

I don't talk about the other reporting and non-reporting traders much because their positioning is usually not paramount in determining price movement. But as that changes, I must as well. While technical fund short selling is still the pure rocket fuel type of buying that I represent it to be, the next best type of rocket fuel buying results when the other reportable and non-reportable traders take a plunge on the short side, as is evidenced in this week's report. In my experience, the emergence of new short sellers joining with the technical fund shorts creates more fuel to what looks like a coming bonfire of the shorts.

In COMEX silver futures, the total commercial net short position declined by 1700 contracts, to 12,400 contracts, a level only lower on two occasions in the past year. Considering the extreme price weakness during the reporting week, I was looking for more of a reduction in the commercial short position in silver. All things considered, I believe there wasn't much blood left to wring out from the stone.

In somewhat of a twist from the recent mix, the raptors actually sold out 1500 contracts of a net long position still formidable at almost 41,000 contracts. The big commercial buying was mostly by the big 4 (read JPM) in reducing silver shorts by 2800 contracts and 600 short contracts bought back by the big 5 thru 8. In contract terms, this is the second lowest big 4 concentrated short position in years and by percent of total open interest, the 19.4% held short by the big four is a percentage lower than any of my available records indicate.

In combination with the Bank Participation Report, in appears to me that JPMorgan holds no more than 8000 to 9000 contracts net short in COMEX silver futures. This is by far the lowest amount of silver held short by JPMorgan and a landmark figure that had been four or five times higher at times over the past 6.5 years (since JPM acquired Bear Stearns). No one should be surprised that JPMorgan's short silver position on the COMEX is at its lowest at precisely the same time that the price silver is at its lowest level in more than 4 years. After all, getting JPMorgan's short position this low could not be accomplished without silver prices being this low. Something very strange and unusual occurred to me Â? unless JPMorgan increases its COMEX silver short position dramatically on the next silver rally (now long overdue) Â? I just may have to stop referring to them as crooks, as hard as that is to believe. Oh well, I guess I'll always have the CME Group as a backup.

Where I was off the most in this week's COT predictions, was in the technical fund department. Where I had envisioned a jump in the short category of managed money of 5000 contracts or so, this short position was reduced by nearly 1900 contracts. Some of the technical fund shorts appear to have cashed in on some very large profits, as has occurred in the past. But, at more than 44,000 contracts gross short, more than 95% of the buying rocket fuel remains intact. And remember, the now-near record technical fund short position must be maxed out at some point and it's more than possible we've passed the maximum number of contracts that can be shorted by the technical funds. In the end, that's the purpose of focusing on record extremes Â? because records suggest the maximum position may be at hand.

As was the case in gold, there was notable net selling by the other reportable traders and non-reporting traders of a combined 6000 contracts, including 3500 contracts of new short contracts. Overall, the buying back of shorts rocket fuel actually increased when all speculative trading categories are considered. Also of note was the increase of more than 2300 contracts on the long side of the managed money category, which I first noticed early this year. I still consider these traders to be value oriented and unlikely to sell on still lower prices as would seem to be evident in their buying on the sharply lower prices of the reporting week.

The COT structure has been and continues to be extremely bullish for gold and silver (and other COMEX/NYMEX metals). It's hard for me to see how it could get more bullish, but I've said that before only to see things get more extreme. The high volume trading since the Tuesday cut-off, which featured sharp new price lows and an equally sharp bounce back in gold makes handicapping what took place in positioning difficult, but it's hard for me to imagine any great increase in commercial selling, particularly in silver. The resolution still lies ahead and there is nothing in this week's report that suggests the resolution to the upside will not be dramatic.

I'm traveling back to Florida over the next few days, so while there may be a delay in publishing Wednesday's report, I'll do my best to make sure I get out a report on that day.

Ted Butler

November 8, 2014

Silver – $15.80

Gold – $1178

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