A Sure Thing?

No analyst should be as presumptuous as to term any future circumstance as a sure thing; hence the question mark. There is a difference, after all, between analysis and prophecy. However, a sure thing describes how I feel about the future prospects for much higher silver prices from current levels. Most importantly, I will try to explain why silver looks good to go much higher over time.

Admittedly, this is not the first time I have felt strongly about silver and, in fact, I used this very same title six years ago, on November 18, 2008. The price of silver would slip to $9.17 (on the London Fix) three days later and has never been lower since; having climbed five-fold by April 2011, two and a half years later. Even after the horrific price beating since the top over the past three and a half years, silver still sits close to double the level it stood at in November 2008. http://news.silverseek.com/TedButler/1227032447.php

Those were dark days for silver investors (although not for buyers) in November 2008, perhaps as much as present times. Back then, silver had collapsed by more than 50% in less than four months and was at the lowest price levels in several years. At the time, many were predicting silver would collapse further to the $5 level it had been at not that many years before. Very few envisioned a dramatic price rise in relatively short order; fewer still publicly wrote about it.

To be fair, I didn't turn super bullish on silver suddenly in November 2008. As always, it was more of a process based upon the usual things I look at, namely, the supply/demand fundamentals and futures positioning on the COMEX. The truth is that I started getting super bullish on silver several dollars higher in 2008, as silver collapsed from over $21 in March (when Bear Stearns, the big COMEX gold and silver short was acquired by JPMorgan) to the low at $9. All that said, I did write that silver was a sure thing in the low nine dollar range in 2008 and it has never been lower than that since. Sometimes you get it right; not all the time, but sometimes.

In reviewing that old article I was struck by my mention of JPMorgan as the big COMEX silver short, as I had in several articles around that time. In fact, I had just uncovered that JPMorgan had taken the mantle of big silver (and gold) manipulator from Bear Stearns and I was the first to state so publicly. Nowadays, it's a given that JPMorgan is the big silver price crook. I was also struck by my price prediction of $20 to $30 or much higher prices should sufficient physical tightness appear. As long time readers may be aware, I'm reluctant to mention specific price targets, particularly by specific dates as that detracts from the reasoning behind the price prediction. Besides, if anyone could consistently pick prices and times, why would he need to write about it? But in this case, silver was so extremely undervalued that I felt it was necessary to suggest by how much.

As always, my main belief for why silver looked like a sure thing back in late 2008 was a combination of physical market factors and futures positioning on the COMEX. Specifically, I wrote that the big COMEX commercial shorts (led by JPMorgan) had succeeded in forcing prices lower and this intentionally generated speculative long liquidation which enabled the commercials to reduce their net short position to the lowest levels in years. Then, like now, silver (and gold) prices only fell because the COMEX commercials wanted to buy and when they were finished buying prices would rise.

On both counts, physical market considerations and COMEX positioning, silver actually looks better today than it did in November 2008. I recognize that prices are substantially higher today than they were in late 2008, but that is neutralized by the improvement in relative conditions and market structure today. Let me cover COMEX futures positioning first.

At first glance, the Commitment of Traders Report (COT) looks marginally better today than it did back then from a conventional perspective. And that's saying something since November 2008 proved to signal a price bottom that has held to this day. In other words, we have less of a commercial net short position and less of a non-commercial net long position in COMEX silver today than we had on November 18, 2008. Likewise, the concentrated short position of JPMorgan and the 4 largest traders is less in silver today than it was back then. But these marginal improvements are not what make the current set up so spectacular to me. Rather, the current set up is spectacular when you look at it in the manner I have gravitated to over the past couple of years — by looking closely at the managed money category.

In effect, the emergence of the technical funds on the short side of silver (and gold and other commodities) over the past two years has transformed a marginal improvement into something so spectacular that I can hardly believe it has occurred. Simply put, the headlong rush by the technical funds onto the short side of silver (and gold and copper) has created the opportunity for a price explosion that didn't exist in 2008.

Yes, there is still a large short position held by 8 or less commercial traders in COMEX silver, although that position is much closer to historic lows than historic highs. But what makes today's set up so much more spectacular than what existed in 2008 is the current unimaginatively high and record number of technical fund shorts. In 2008, the CFTC wasn't yet publishing disaggregated data, so some allowances must be made.

At the price bottom in 2008, the total non-commercial short position (and that includes both managed money and other large reportable traders) was less than 11,000 contracts. The current COT report indicates that more than 44,500 contracts (222 million oz) are held short in the managed money category alone. In other words, the technical funds are short 4 to 5 times more silver contracts today than they were short on November 18, 2008. In less than three months, the technical funds have sold short 36,000 additional contracts (180 million oz) of COMEX silver. (For those curious about gold, the technical funds appear to hold twice as many short contracts as they did on November 18, 2008, similar in pattern to silver's configuration, just not as extreme).

This represents a revolutionary change in the COT structure from what existed in 2008 and is the prime component in my silver is a sure thing premise. I'll spare you my arguments about why it is so crazy to allow purely speculative traders to sell or buy such massive amounts of contracts in unison that it necessarily distorts the price. In any event, the massive short selling by the technical funds has already occurred and that is why silver prices dropped more than 20% in less than three months. But short sales are open positions and, particularly in the case of the technical funds, all those shorted contracts must be bought back at some point.

Even though I have been convinced all along that the commercial traders, like JPMorgan, lead the technical funds into and out from the market thorough the commercials' control on price; I am amazed at what the commercials have accomplished. Up until very recently, I would have not believed that the technical funds would ever hold such record extreme short positions in COMEX silver (and somewhat similar short positions in COMEX gold and copper).

So a very big factor in me resurrecting the sure thing premise and something not in force at the 2008 bottom is the current extreme short position held by a group of traders with no choice but to buy those short positions back at some point. In addition to the 35,000 to 40,000 short silver contracts that must be bought back by the technical funds, there will likely be an additional 15,000 to 20,000 contracts of new longs sought to be purchased by these same technical funds on any upside penetration of the key moving averages.

By my count there is an imbedded total of 50,000 to 60,000 net contracts of buying power in COMEX silver by the technical funds alone on a $2 to $3 move up in price. In terms of equivalent silver that comes to 250 to 300 million ounces that must be bought eventually. A large part of my premise of higher silver prices rests on the inevitability of the coming technical fund buying and its resultant impact on price. The certainty of large and aggressive technical fund buying at some point is what makes silver a sure thing.

Of course, while very different from the set up in 2008, the current market structure set up is not all that different from what has existed on several occasions in the recent past, including at year end and in June of this year. On these occasions and others when the technical funds held a large short position in silver, the set up always resulted in a rally, but those rallies were limited and capped by aggressive commercial selling. Therefore, I can't rule out that not occurring again; although I am convinced it cannot recur indefinitely. One day, the COMEX commercials will not cap silver prices and nothing precludes that day not being at hand.

Even if the commercials cap the next silver rally that does not automatically negate the sure thing premise, as silver prices must move higher before they may be capped. More importantly, silver prices have been driven so low that interference from the actual world of metal fundamentals looks set to occur. I discussed the effects of silver being below the cost of primary mine production in the original article, but this time it is way different.

Silver dipped to $9 in 2008 for what, in retrospect, was a brief moment. On the other hand, the plummeting of silver prices has lasted for years this time, including a year and a half locked around $20 or less. While actual silver mine production hasn't fallen off yet, I don't know of an exploration or development budget that hasn't been adjusted downward as a result of the continued depressed price of silver. It may be hard to quantify how much future silver production has been delayed or eliminated completely, but based upon the stock prices and re[ports from silver mining companies, it is no small amount.

Compared to the fundamentals in 2008, current fundamentals for silver look more compelling, both from an industrial demand and investment viewpoint. And from the sources that can be verified, there seems to be more relative investment demand for silver compared to gold. From ETF flows to official coin statistics, silver appears to be the standout.

A favorite theme of mine for the past three and a half years has been the extraordinary and unprecedented physical movement of metal into and out from the COMEX-approved silver warehouses. In 2008, it would be years before that turnover commenced. Yes, the world has mined more than 4 billion oz of silver over the past 6 years, but more than 90% of it has been consumed or put into forms not likely to return to the market. The frantic movement of physical silver today suggests an overall wholesale tightness that didn't exist in 2008 (although there was very strong retail investment demand back then).

The hot growing industrial use for silver is in the production of solar panels to generate electricity. In 2008, the solar industry was in a relative state of infancy compared to where it is today. The projections that I see for the future use of silver in solar suggest that we will look back at this time the same way we look at 2008, namely, staggering growth from this point as well. In 2015, the Silver Institute estimates 100 million ounces of silver will be used in solar panels, many times the amount used in 2008. Future projections indicate the world will consume many times current elevated levels.

Just this week, the Nobel Prize for Physics was awarded to three scientists for

perfecting LED light technology which promises to benefit billions around the world in energy savings and, in conjunction with solar technology, in introducing a light source apart from kerosene-burning lanterns. This appears to be a truly well-deserved award for something that will benefit mankind.
http://abcnews.go.com/Technology/wireStory/japanese-american-win-nobel-prize-physics-26011349

A few months ago, the Silver Institute published a technical report on silver and its use in various new applications, including LEDs. I don't recall similar Nobel Prize awards or reports about silver in LEDs back in 2008. It's simply amazing how silver is being used today compared to back in 2008.
https://www.silverinstitute.org/site/wp-content/uploads/2014/07/NEEUof-Silver2014.pdf

Of course, the most important demand for silver in terms of price performance is investment demand. Given the limited amount of silver available for investment after deducting total fabrication demand from mine and recycling supply, it would appear to be only a matter of time before investors bring about a real pinch in total availability. Against a very finite availability in actual physical silver supply, now contemplate the many trillions of dollars and other currencies created throughout the world since 2008. More money and buying power has been created over the past six years than ever before in the human experience. Thanks to an incredibly low price, the mismatch between buying power and the amount of actual silver that could be bought is much greater today than ever before.

All this is why silver looks like a sure thing to me (yet again). But I urge you to not focus on my opinion, but look to the facts yourself. What matters is what you think. I'm convinced that silver looks as close to a sure thing as is possible, but I can't invest in it for you. That's something you have to do yourself.

Ted Butler

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Silver – $17.30

Gold – $1217