

September 27, 2014 – Weekly Review

Weekly Review

This week's precious metals ending was noteworthy, even if the net change wasn't large, as gold finished \$4 (0.3%) higher, while silver ended lower by 15 cents (0.8%). More of note is that in the past eleven weeks, silver has only managed one slight up week; gold fared better with three slight uptick weeks. Over this time, silver has fallen by close to \$4 (18%) to a series of new four year lows. In the same 11 weeks, gold shed \$120 ((9%) and erased this year's gains. When I think about the notable changes in the actual supply and demand for these metals to explain the sharp decline (away from COMEX positioning), I come up blank.

As a result of silver's relative underperformance to gold, the silver/gold ratio widened out another full point to over 69 to 1, not coincidentally, also the highest level in four years. There is a two-fold meaning that silver is cheaper than it has been in four years, both on an absolute basis and relative to gold. Admittedly, it means that anyone holding silver on the ride down (including me) has suffered mightily on existing holdings. But it also means, if you are a long term value investor who happens to believe the facts surrounding silver, that this is the best time to buy silver in more than four years – either for cash or by using gold as a source of funds.

Just to be clear and as I hope I have conveyed all along, my suggestion to sell gold to raise funds in which to buy silver only applies if you have gold and no cash or any other assets to convert. It certainly doesn't mean I think gold is going a lot lower; to the contrary, I think gold looks poised to rally sharply, based upon the COT market structure on the COMEX. Then why would I suggest selling it to buy silver? Simply because I believe you will get a much bigger bang with silver without any bigger risk than holding gold at this point.

In the interest of full disclosure, if I owned any gold I would sell it to buy silver; but I don't own any gold and never have (although years ago I did trade in gold options from time to time). I've never understood the supply/demand fundamentals in gold as well as I believe I understand them to be in silver. Based upon that understanding I see a physical shortage coming in silver that I don't anticipate coming to gold. Physical shortage is the most powerful force for an upside explosion in a commodity's price known to man. Plus, I'm convinced the ongoing manipulation has impacted silver more to the downside and that will end one day and provide an additional source of fuel to the upside. I'm not getting into all the merits for holding silver in place of gold today, but favoring silver has nothing to do with my expectations of the future direction of gold prices.

One of the indisputable facts regarding physical silver is the continued daily movement of metal into and out from the COMEX-approved warehouses. This week, nearly 6.5 million oz were moved in and out, well above the already high 4.5 million oz average weekly turnover this year. Total COMEX silver inventories rose a substantial 2.7 million oz to 183.4 million oz, up about 8 million oz from year end and at a 15 year high. (The all-time high in COMEX silver inventories was over 280 million oz back in the mid-1990's).

Invariably, growing inventories in a commodity are assumed by many to represent a surplus of supply over demand and, therefore, be bearish to price prospects. The ironic thing is that COMEX silver inventories hit the high of over 280 million oz around 1995 while the silver market was deep into a 65 year structural supply deficit – which meant there was less silver in the world each year for 65 years (thru 2006). In retrospect, it's easy to explain how COMEX silver inventories grew to such high levels in the face of a documented depletion of world inventories, although few (including me) knew this at the time.

The explanation was that silver inventories were being built on the COMEX due to warehouse consolidation and as a result of central bank leasing of silver at the time. Thus, even though there was less silver in the world each year for 65 years running, enough was shuffled into the COMEX warehouses for other reasons that COMEX stocks climbed sharply to all-time highs. COMEX silver inventories are a subset of total world bullion inventories and a change in COMEX stocks might not reflect what is happening to total world inventories. My point is that one shouldn't equate growing inventories as only a sign of surplus, as there may be other explanations for why COMEX (or SLV) inventories would grow.

Today it's different than it was in 1995. Silver hasn't been in a structural supply deficit since 2006, meaning that there has been more silver in world inventories each year for the past 8 years than there was in the preceding year. Therefore, it should be expected that COMEX and SLV inventories would grow as these are two prime places where investors store silver.

The important point is that the depletion of world silver inventories for the 65 years that ended in 2006 was so severe that even a hundred years of surplus wouldn't restore the 9 billion oz of world inventories already depleted. I would also remind you that silver soared to nearly \$50 in 2011, five years after the silver structural deficit ended and world inventories started to grow. If growing inventories were negative to silver's price performance into the highs of 2011, let them be negative again. I still think the turnover is more important than the totals – it's not the ocean, it's the motion.

Certainly, the holdings in the big silver ETF, SLV, are growing. This week, nearly 6 million oz were added to the trust, making the monthly increase almost 15 million oz and the total since June more than 25 million oz. Considering the rotten silver price performance and a corresponding outflow in the big gold ETF, GLD, the inflows into SLV are impressive and thought provoking. There was some slight reduction in the short position of SLV for the period ending September 15, but the 570,000 share reduction in a total short position now near 13.7 million shares (oz) short does not fully explain the growth in silver metal holdings in the trust. Although, I must point out that this is the lowest SLV short position in months and at 3.8% of total shares outstanding does not appear to be a great influence on price. Still the SLV short position must continue to be monitored.

<http://shortsqueeze.com/?symbol=slv&submit=Short+Quote%99>

So why is so much silver flowing into the SLV, particularly in light of the lack of gold flowing into GLD and the crummy price action? I can't uncover or imagine a sinister plot by the bad guys (aka the collusive commercials on the COMEX) and by process of elimination must assume it represents value buying motivated by the incredibly cheap price of silver. Plus, the buying in SLV looks widespread since no large buyer has revealed a 5% holding (18 million shares) yet and we have not seen a conversion of shares to metal which would suggest a large buyer was seeking to shield his identity. If the large recent deposits of metal into SLV are bearish in any way, I can't see it.

Starting a couple of weeks ago, sales of Silver Eagles from the US Mint started to pick up after a few months of relatively weak sales. At this point, I'm not sure if the pickup in sales is a general pick up in retail demand (as appeared to be the case this week) or a return of "Mr. Big." The easiest way to measure the sales pace is to convert interim reports from the Mint into a daily run rate by dividing total sales as they are reported by the number of calendar days on the date reported. Looking at the current data, the daily run rate as of yesterday was 117,000 coins a day, which if maintained would equate to 3.5 million total sales for September and getting back to the strong levels of earlier in the year. Sales of Gold Eagles have also increased notably, no doubt as a result of the mark down in price.

http://www.usmint.gov/about_the_mint/index.cfm?action=PreciousMetals&type=bullion

As is usually the case, this week's Commitments of Traders Report (COT) was mostly expected (with one notable exception) and explained price action during the reporting week. Not only did we make a series of new price lows in COMEX gold and silver, new price lows occurred in COMEX copper, as well as NYMEX platinum and palladium. Since common supply/demand explanations are missing as to what would account for the remarkably similar price performance of these five separate and distinct metals, the explanation must lie elsewhere. I'll return to this theme in a moment.

In COMEX gold futures, the commercials reduced their total net short position by 11,900 contracts to 64,300 contracts. This is the lowest (most bullish) commercial short position in gold since the June price lows. In the five reporting weeks since August 12, the commercials have reduced their net short position by 96,000 contracts (9.6 million oz) on a \$100 drop in the price of gold. The commercials always buy big on big price declines, so some might say they must be incredibly good traders or are the luckiest sons of guns in the world. I would say that it has nothing to do with anything good or lucky; this repetitive result can only be due to the game being rigged.

By commercial category, it was all raptor buying, as the big 8 added 3000 new shorts and the raptors bought close to 15,000 gold contracts. Even after the new short selling by the big 8, the gold concentrated short position is still very much on the low (bullish) side. Somewhat surprisingly, considering the pronounced raptor buying, JPMorgan stood pat again at 25,000 net long gold contracts.

On the speculative sell side in COMEX gold, the technical funds (in the managed money category) accounted for most of the commercial buying of 11,900 contracts by selling more than 10,000 contracts net, including almost 7000 new short sales. This puts the gross short position in managed money with a few thousand contracts of the 83,000 contract record technical fund short position of last December. Also noteworthy this week was a fairly sizable liquidation of more than 4000 contracts from the non-reporting (smaller) traders, highly suggestive of capitulation and a final wash-out.

With further improvement since the Tuesday cut-off, gold looks good to go on the upside, whenever the deliberate move down runs out of fuel. Despite the bullish gold set up, I would still switch to silver.

In COMEX silver futures, the total commercial net short position declined by a hefty 6,800 contracts or the equivalent of 34 million oz, or about as much as the US mines in a year. At 16,800 commercial contracts net short, there have only been a handful of weeks over the years where the silver short position has been lower. On all those previous occasions, a significant market bottom was recorded and a rally followed. It shouldn't prove any different this time.

By commercial category, the big 4 bought back 1500 short contracts and the big 5 thru 8 bought 500 short contracts as well. The raptors (smaller commercials) added 4800 contracts to a net long position now just shy of 40,000 contracts. Whenever the raptors have held more than 40,000 COMEX silver contracts net long, it was always just a matter of time before a rally unfolded.

I would peg JPMorgan's concentrated short position to now be down to 11,500 contracts, the lowest since acquiring Bear Stearns' short position more than six and half years ago. Any lower and it will probably be too hard for me to calculate this crooked bank's silver short position; a day I have long hoped for. However, the day I have most hoped for is the day JPMorgan refuses to add to silver short positions on any rally and that day is still just a hope at this point.

There is no question that JPMorgan and the other collusive COMEX commercials have manipulated prices lower to buy the impressive quantities of contracts reported in the COT reports; but the bigger manipulation has always been the selling of contracts on price rallies for the express purpose of capping prices. I know these crooks have always sold on rallies, but I also know that can't continue indefinitely. Somewhere between what they've always done and what they can't do in the future lies the rally not to be missed.

It was on the speculative sell side of COMEX silver that the one big surprise of the COT report occurred. The technical funds in the managed money category didn't account for any of the 6,800 contracts that the commercials bought. In fact, the managed money category actually bought on a net basis 600 contracts, including buying back 1600 short contracts. Since I had been expecting the tech funds to have sold as many as 6000 new silver shorts on the price weakness during the reporting week, it would be no exaggeration to say I missed by a country mile. Despite the wide miss, this doesn't change things much. Please allow me to explain.

At more than 40,000 contracts still short in the managed money category, the technical funds are still very close to the previous record short position of nearly 43,000 contracts, so the vast majority of the rocket fuel of technical fund short covering is still intact. If anything, this tends to confirm my approach of using the most recent COT extreme as a limit for guessing the extent of future extremes.

And as I indicated on Wednesday, technical funds can make money individually if they break away from the collective technical fund position early. As a result of the steep silver price decline, we have moved deeply below the moving averages. This means there is a larger risk of the technical funds losing their collective open profit if prices rally soon and this obviously motivated the technical funds which did cover in the reporting week. So, all in all, the technical fund short covering this week is not of prime concern.

But if the technical funds didn't sell at all, who was on the sell side that permitted the commercials to buy 6800 silver contracts? As it turned out, it was the non-reporting (smaller) traders which provided net selling of 4700 contracts. Upon reflection, this makes sense since silver did hit a series of new price lows during the reporting week, including a decisive penetration of the \$18 mark, for the first time in four years. Remember, COMEX futures contracts are held on margin and most long holders were subject to margin calls and the emotional stress of losses piling on open losses. As was the case in gold, this strikes me more as a sign of final capitulation than anything else.

In fact, early this week, I received an email from a long term subscriber, asking about the possibility of such a liquidation in the non-reporting category. I told Shailendra that it was possible for there to be such a liquidation and threw out the potential for 5000 contracts as possibly being sold. (He asked if 5000 to 10,000 contracts might be sold). At that time, I was still expecting further technical fund short sales, but after ruminating on the new report and what transpired price wise, the overall picture still looks extremely bullish to me. But that was a timely note from a subscriber paying close attention.

Let's return to the theme that all five primary COMEX and NYMEX metals were sharply lower during the reporting week and remember that these are all very different metals with different supply demand circumstances. Therefore, it is virtually impossible that all five metals — silver, gold, copper, platinum and palladium — all witnessed supply/demand developments responsible for the simultaneous price declines in all five. Something else had to account for all five metals declining sharply. Something else did.

Please take a moment to look at the disaggregated COT report this week. Even though I already discussed that silver broke the pattern of technical fund net selling being the prime cause of the price decline in the reporting week, the other four metals exhibited a stark similarity in that the managed money category in gold, copper, platinum and palladium all featured big long liquidation and an increase in short positions to the point where the net selling in the managed money category accounted for more selling than any other category.

http://www.cftc.gov/dea/futures/other_lf.htm

What this proves is that the collusive commercial trickery of the technical funds, so prevalent in COMEX silver for years, has now spread to all the COMEX metals. Actual supply and demand has been pushed aside in price discovery considerations and has been replaced by crooked dealings on exchanges run by the CME. That's because the quantities of contracts dealt with on the COMEX and NYMEX far exceed the quantities of actual materials being transacted over similar periods of time. And since we know that participants in the managed money category are purely speculative (as are their commercial counterparties), the price of silver, gold, copper, platinum and palladium is being set and manipulated by speculators. This is so against the intent of US commodity law so as to embarrass the crooks at the CFTC and CME. (I would imagine, based upon the regulatory record that the crooks at JPMorgan are beyond being embarrassed).

One of the bright points is that this situation can't last indefinitely. At some point, the producers of the world, be they big mining companies or big mining countries, will wake up to this scam being perpetrated on exchanges run by the CME. Now that we're at such a bullish structure in silver and gold (yeah, we can always get more bullish) that means the scam is becoming clearer. I just can't see how this overt manipulation can be ended on a gradual basis at this point because it is so advanced. Maybe the COMEX and NYMEX commercial crooks will again sell aggressively on the next rally, whenever that comes (I think soon), but one of these days they will stand aside and let silver prices seek free market levels. I've always been convinced that day will come when the commercials are as least short as possible. Like now.

Ted Butler

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Silver – \$17.65

Gold – \$1220

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