April 27, 2022 – Sudden Changes

There were a number of sudden changes of late â?? not limited to the plunge in silver and gold prices â?? that I planned on discussing today. One of the planned topics included a discussion on the state of interest rate derivatives as reported in the Office of the Comptroller of the Currencyâ??s quarterly report. Despite being beaten to the punch by the cracker jack team at Wall Street on Parade (Pam and Russ Martens), Iâ??ll press forward, since I referenced the topic previously â?? before some rather stark and sudden changes in interest rates.

https://wallstreetonparade.com/2022/04/fed-chair-powell-telegraphs-the-perfect-storm-for-wall-streets-megabanks-rapid-rate-hikes-hitting-234-trillion-in-derivatives/

Back in the Weekly Review of Jan 15, I included a separate section anticipating how the OCC might respond to my questioning of it to explain the massive increase in the precious metalsâ?? derivatives position of Bank of America as of Sep 30, 2021 â?? a position that continued to grow sharply in the subsequent new report for positions as of Dec 31. â??Anticipated responseâ?• is still the operative term, since no response has been issued by the OCC yet.

Generally, I anticipated that the OCC might respond by downplaying my concerns that Bank of America had assembled what might be, in effect, a massive short position on silver of perhaps 800 million oz by pointing out that, compared to interest rate derivatives, precious metals derivatives were a drop in the bucket in notional dollar terms – a multi-billion-dollar affair compared to the hundred or two hundred trillion-dollar notional value of interest rate derivatives.

I attempted to show how comparing interest rate and precious metals derivatives was like comparing apples to oranges, namely, that this was an inappropriate comparison because the risk on interest rate derivatives was far less than the risk on precious metals derivatives because the full value of the underlying interest rate instrument was included in the notional value â?? even though the actual risk was infinitely less on interest rate derivatives than on precious metals derivatives. To be clear, what I was attempting to do was to cut the OCC off from making a false and misleading comparison.

However, interest rate conditions â?? which I cited as barely moving for years (which was true enough up until that time â?? Jan 15), suddenly embarked on what has turned out to be the sharpest rise in several decades. Therefore, I must sit up and take notice of the drastic increase in interest rates since I wrote about them more than three months ago. Not to the point where it undermines my basic argument that comparing interest rate and precious metals derivatives is like comparing apples and oranges, because thatâ??s still true.

Why the sharp increase in interest rates over the past few months (particularly the past month) bears mentioning is the heightened risk of a financial â??accidentâ?•. Yes, Iâ??m well-aware that on a long-tern basis, even after the recent sharp increases, interest rates can hardly be considered high on a historical basis. I cut my teeth on the interest rates of the Paul Volker era, so itâ??s hard to view interest rates below 3% across the entire US Treasury yield spectrum as being excessively high.

But, when it comes to derivatives, even more important than the absolute level of interest rates is the rate of change. And what we have witnessed since I wrote about interest rate derivatives back of Jan 15 is nothing less than perhaps the largest percentage increase in history. Moreover, if the Federal

Reserve sticks to its guns in its fight against surging inflation, there are further sharp interest rate increases in store.

The problem is that considering the gargantuan size of both the OTC derivatives market covered in the OCC report monitoring US banks, plus the equally massive size of the listed market in interest rate derivatives, the extremely large rate of change in interest rates is akin to setting a match to a mountain of dynamite. Â Add in the extremely concentrated nature of the derivatives holdings of a few large banks and this only enhances the chance of a financial accident of historical proportions. Worse, given the highly opaque nature of the OCC report â?? where no specific positioning or counterparty data is made clear â?? and it almost guarantees that if some entity or entities fail, it will only be made clear after the fact.

Remember, there is both a long and short holder for every derivatives contract in existence and sudden sharp moves create winners and losers, as this is a zero-sum game. Itâ??s not the winners that cause financial problems – thatâ??s the province of the losers. For past examples, think of Bear Stearns, Lehman Bros. and AIG, when the problems only became obvious largely after the fact and too late to address.

So, while I still find any attempt at comparing interest rate and precious metals derivatives positions to be bogus, the rate of change in interest rates combined with the massive amounts of such contracts in existence creates a whole new set of threats to financial stability. Here, I would whole-heartedly agree with the Martens that prospects of this just might be weighing on financial markets of late. The connection with silver in all of this is to heighten its appeal as a safe haven asset â?? not something on my mind back on Jan 15.

Perhaps more than anything else, it alarmed me that (before it was discussed in WSOP) I had seen absolutely no attention placed on this matter. There are too many visible threats to financial system stability, not the least of which is the almost unthinkable developments of the war in Ukraine, including the ease in which Russia now throws around the possibility of nuclear weapons deployment. Still, the history of â??Black Swansâ?• suggests the most dangerous are those that arrive and land almost without notice.

Another sudden change is the emergence of Elon Musk as offering to take over and making privately-owned, the social media site Twitter. I have no insight or comment on whether the attempt will prove successful or even advisable, as I have no strong feelings in any regard. So, please bear with me for a moment while I make my own apples to oranges comparison with silver.

The first connection with Mr. Muskâ??s takeover is the size of the deal, roughly $45 billion, which happens to be within spitting distance of the value of all the silver bullion in the world in 1000 oz bar form (2 billion oz) at current prices. Comparing this same relative value with silverâ??s most relevant precious metals companion, gold, the value of all the gold bullion in the world of some 3 billion oz (half of all the gold that exists in all forms) is close to $5.7 trillion about 125 times more than either the value of Twitter or all the silver bullion in the world. No knock on Musk (or anyone else) but this is a dollar amount beyond reach by any individual, from the worldâ??s wealthiest on down.

Of course, while the bid for Twitter looks doable, any bid for all the silver bullion in the world at a comparable premium (say $30 an oz) would attract far, far less than all the Twitter shares likely to be tendered. Quite literally, should anyone or any entity succeed in buying all the silver bullion in the world and converting it to private ownership, the world as we know it, would no longer exist (Noting that JPMorgan & friends already own half of all the worldâ??s silver bullion). With all the worldâ??s silver converted to single private ownership, that would mean no COMEX silver, no silver ETFs, no industry working inventories â?? admittedly a somewhat absurd proposition. Except for the fact that whatâ??s really absurd is the current undervaluation of less than $50 billion for the entire world supply of an indispensable material.

Actually, I had been thinking about Mr. Musk and silver before his recent takeover bid for Twitter. More specifically, I was thinking about the prospects for his electric car company, Tesla, buying a good-sized chunk of silver for the purpose of legitimately hedging the future availability and cost for a vital component of electric (and non-electric) vehicles. Tesla has made similar arrangements for nickel, lithium and cobalt, to my knowledge and such a deal in silver or silver miners seems quite sensible to me.

Certainly, Iâ??m not speaking of Tesla or anyone attempting to buy all two billion ounces of silver in the world, but something on the order of 50 or 100 million oz. I donâ??t think anyone would argue that both silver and Mr. Musk have a certain special panache that if combined could cause a powerful impact on price. On two previous occasions, with what I believe was my influence in convincing Warren Buffet to buy silver around 1997 (by my writings on leasing) and JPMorgan starting in 2011, the purchases were made with no expectations of same by me. If Musk or Tesla end up buying silver or a silver producer(s), this is my claim for a finderâ??s fee – hopefully significant enough to donate to the charity of Teslaâ??s choice.

Turning to the sudden sharp selloffs in silver and gold, I hope subscribers know full-well that the selloffs were completely pre-planned and orchestrated and on a retrospective basis, written in stone.Â In other words, while there was some question beforehand as to whether the collusive COMEX commercials could pull off yet another orchestrated and artificial selloff, due to offsetting and near-overwhelming real-world conditions, that question is now answered.

Iâ??m pretty sure subscribers werenâ??t completely caught off-guard by the sudden price swoon. In fact, I received a note of encouragement from one urging me to keep the faith and not to let the bad guys get me down â?? an absolute first and greatly appreciated.

While I would never understate the resultant anxiety and stress imposed on innocent silver investors on each and every deliberate COMEX price takedown, itâ??s more important to grasp what exactly happened and what that means going forward. As sure as the sun rises from the East and sets in the West, we know that certain things are part and parcel of every significant silver and gold selloff on the COMEX, particularly when key moving averages are penetrated to the downside (as was the case on this selloff).

We know for a certainty, for instance, that this weekâ??s Commitments of Traders (COT report will feature significant commercial buying and managed money and other non-commercial selling. We know this because this is the cornerstone of the ongoing, decades-long price manipulation in silver (and gold). The commercials always buy on significant selloffs because many managed money and other technical traders always sell on sharp price selloffs.

The collusive commercials know this better than anyone and thatâ??s why they spoof (now without immediately cancelling their phony sell orders) and deploy other essentially illegal trading tricks to artificially depress prices at key points to get the brain dead technical traders to sell â?? all while the regulators at the CFTC and CME Group take tea and crumpets and pretend not to notice what is obvious to all.

But please donâ??t take this as yet another after-the-fact useless complaint about things that canâ??t be undone or that will continue forever, because that is not my intent in the least. Instead, while this most recent price rig may have more to go in gold, itâ??s already pretty advanced in silver. The same subscriber who urged me to buck up, made the comparison of this selloff with the one that occurred in March 2020, but I would remind you that back then silver fell to the incredible relative value compared to gold of 125 to 1, a level never seen in the 3000 years before the birth of Jesus Christ, nor in the 2000 years since.

I do believe I made quite a fuss over silverâ??s near-incredible level of relative undervaluation at the time and by comparison, today's near 80 to 1 ratio to gold has held fairly stable on this selloff and I, for one, am not expecting sharp relative weakness in silver compared to gold (particularly since silver has already penetrated all its key moving averages, while gold has not).

Much more importantly, there are more reasons than I ever recall that point to much higher silver prices ahead â?? all standing in stark contrast to the one bearish factor that drives prices, namely, collusive commercial positioning on the COMEX â?? which, at some point, also turns into a bullish factor whenever the commercials succeed in wringing the final pound of flesh from willing non-commercial sellers. In fact, important new bullish factors in silver seem to turn up daily.

Yesterdayâ??s release of the new short report on securities is a case in point. Although I had to, quite literally, force myself to refrain from offering any hint of what I expected the short position in SLV, the big silver ETF, to be as of the close of business as of April 14 â?? due to what I admit is a miserable track record in handicapping this report (made only slightly less awful by the lack of any attempt by anyone else to even ever venture a guess) â?? Iâ??m happy to admit I would have been dead wrong again. But itâ??s not merely the avoidance of what would have been yet another embarrassingly wide-of-the-mark call that makes me happy â?? I canâ??t call the unexpected and shockingly large increase as anything but bullish.

Where I would have bet dollars to donuts that following the prior reportâ??s sharp reduction in the short position on SLV (of 8 million shares), there would have been another sharp decline in the short position (due largely to the 12 million oz of physical silver that was deposited into the trust over the reporting period), instead the new report indicated a very sharp increase of nearly 11 million shares to just under 41 million shares (ounces). This is the largest short position in years on SLV.

https://www.wsj.com/market-data/quotes/etf/SLV

When the previous short report was published, I opined that the reduction most likely indicated that BlackRock, the trustâ??s sponsor, had finally taken up privately the issue of excessive shorting on SLV, in which the change in the trustâ??s prospectus in Feb 2021 warned the short sellers to watch themselves. Clearly, in hindsight, no such epiphany took place at BlackRock in light of the massive increase in the short position. And yes, I do plan to petition BlackRock on this issue, if the next short report doesnâ??t indicate a sharp reduction. I was sort of hoping to first get a response from the OCC via my congressman on the Bank of America derivatives position, which is now at the one-month mark.

All that aside, why would I find the large increase in the short position on SLV to be shockingly bullish? Well, for one thing, any large short position is inherently bullish once it has been established. A short position has a price depressing influence as it is being established (sold), of course, but once it is completed, the bearish impact is spent. This is the universal effect of short sales on any asset, including SLV.

But SLV is also a highly unique security in which short sales can closed out by either the buyback of shares on the open market (as is also true in the short sale of any security) or by the deposit of physical silver for conversion into shares, then used to close out the short sale. It is this metal to share conversion process (or vice versa share to metal conversion process) that is unique to SLV and other hard metal ETFs, like GLD, and that makes these securities unique.

In any event, in order to close out a short position â?? which are always considered â??openâ?• transactions as compared to a sale of securities previously owned â?? some form of buying is required that will have a bullish effect on price. In the case of SLV, the buying – whether it is a straight open market purchase of existing shares or the purchase of physical metal on the open market that is then converted into shares to close out the short position â?? will have a bullish impact on price.

But hereâ??s why the sharp increase in the short position on SLV is so bullish at this time â?? at least in my eyes. Â The most plausible reason for why whoever shorted the shares of SLV so aggressively within the reporting period was because not enough physical silver was available in the physical market in order to abide by the strict process dictated by the prospectus of depositing enough physical metal to create the (baskets of) shares required to satisfy new buying. Rather than roil and aggravate an already super-tight physical silver market with significant new demands for metal that only sharply higher prices would provide, the short sellers of SLV took the most immediate short cut available of selling short shares of SLV instead.

One way of visualizing this process is to think of the short sellers in SLV as â??paydayâ?• borrowers. You know, the same predatory and abhorrent lending process by which folks of limited means and behind the eight ball have no choice but to borrow at usurious interest rates in order to make ends meet. Only in the case of the payday short sellers in SLV, their desperation does not revolve around meeting daily living expenses, but in continuing to perpetrate the more serious crime of maintaining the silver manipulation by any means possible. Forgive me, but itâ??s hard for me not to despise these crooks and root for their eventual ruin and to wonder how the regulators can sit by and pretend all is well.

Remarkably, the aggressive new short selling in SLV is but another in a long string of extremely bullish signs emerging in the physical world of silver, joining other factors like the hottest retail market ever, the recent large physical inflows into SLV and other silver ETFs and the continued unique and unprecedented (and widely ignored) physical movements in the COMEX silver warehouses. It seems that all weâ??re missing on the silver physical scene is Moses descending from the Mount bearing stone tablets with the inscription â?? â??Buy Silverâ?•.

As to the sole bearish factor â?? collusive COMEX commercial positioning â?? this Fridayâ??s new COT report should give a us a good sense of where we stand, at least as of yesterdayâ??s cutoff for the reporting week. With silver having plunged every single day of the reporting week – for no reason other than to allow the commercials to induce the non-commercials into selling – and the downward penetrating all three key moving averages (quite rare for a single reporting week), the only question is how much and what type of commercial buying occurred.

Iâ??m still very much of the opinion that the commercial game may have changed in favor of the raptors at the expense of the biggest shorts, as I discussed on Saturday. Most important will be how much new managed money shorting may have emerged in silver (and gold) for this week and possibly beyond. My sense is that most of price damage may have been seen in silver â?? based upon the extent of the decline so far and already-decisive moving average penetration â?? with more of an open question on that in gold. Should we get a more concerted price takedown in gold (by no means guaranteed or justified), that might pressure silver lower, but my sense is that silver should not lead gold to the downside from here. I do feel that regardless of whether we move lower still in silver, itâ??s a certainty that it wonâ??t be terribly long before prices trade substantially higher than current prices.

In some (sick) sense, you have to hand it to the COMEX commercial crooks (mostly the raptors) for pulling off yet another manipulative selloff â?? whether it is over with or not. Then again, itâ??s not that great of an accomplishment when you consider the collusive commercials have the regulators in their back pockets. A pox on all of them.

Even though the raptors appear to be mostly running the show (pending review of the new COT report), the 8 big COMEX gold and silver shorts have reaped the largest relative rewards on the sharp price smash in the reduction of their total losses. At publication time, the 8 big shorts total loss was reduced by a further $1.5 billion from Fridayâ??s close, to $10.5 billion.

Ted Butler

April 27, 2022

Silver – $23.35Â Â (200 day ma – $23.94, 50 day ma – $24.99, 100 day ma – $23.93)

Gold – $1887Â Â Â Â Â (200 day ma – $1833, 50 day ma – $1938, 100 day ma – $1872)

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