

April 7, 2021 – Another Piece of the Puzzle

Analyzing the silver market is typically a case of studying the facts that can be uncovered and forming the most plausible explanations around those facts. Often, the facts and explanations are micro or isolated in nature, but later lead to broader or more macro scenarios – sort of like putting the pieces together for an incredibly complex jigsaw puzzle (not something I usually have an infinity for).

Here's a new piece of information I just discovered that seems to fit in with a premise I've previously presented. One caveat with fitting newly discovered facts with past premises is one has to guard against confirmation bias, or seeing things the way you want to see them, instead of how they really are. In this case, it sure seems that the newly uncovered facts so closely match a previous premise, that I am at a loss to come up with a more plausible explanation than the one originally advanced.

The new facts are contained in the latest release of the Treasury Department's Office of the Comptroller of the Currency (OCC) Quarterly Derivatives Report for US banks. The report covers derivatives contracts in the over the counter (OTC) market as opposed to exchange-traded futures and options contracts, like COMEX gold and silver futures. A couple of quirks about the OCC quarterly report include it being delayed about 3 months, so the new report just released on March 23, covers positions held as of Dec 31, 2020 (compared to a three-day delay in the COT report).

The other big quirk in the OCC report is that it only provides holdings by banks on a total notional basis and not whether the banks in question are net long or net short and by how much. That makes the OCC report much less relevant to someone like myself, who examines gross, net and category positions in the COT report with a fine-tooth comb. Compared to the COT report, the OCC report is so fuzzy and nebulous that most don't bother to look at it in precious metals circles. Finally, a change some years back to include gold in the foreign exchange category has made any firm conclusions about gold impossible (at least for me) to analyze objectively (although it does make the remaining precious metals category more specific to platinum and palladium and, particularly, silver). My guess is that the Treasury Department wanted to make gold dealings opaquer and not make silver more transparent, but that's the way it turned out.

All that said, I have been monitoring the OCC report for decades and have been able to uncover a few tidbits from time to time. If you want to check the data on your own, please use this link to download the current and past reports. You'll want to scroll down to table 9 in each report to verify what I'm about to represent.

<https://www.occ.gov/publications-and-resources/publications/quarterly-report-on-bank-trading-and-derivatives-activities/index-quarterly-report-on-bank-trading-and-derivatives-activities.html>

One constant in the report is that JPMorgan dominates and has dominated OTC dealings in every category for as long as I can remember and precious metals dealings are no exception. I did note that a few years back, Citibank emerged as the only other major US participant in precious metals dealings. The new report does indicate that another US bank (foreign banks aren't included), BankAmerica, has emerged as a major participant in precious metals OTC derivatives, nearly matching Citibank's total position. More to the point, BankAmerica's position, at \$8.3 billion (as of Dec 31), has, essentially, come into existence since March 31, 2020, when it was under \$175 million.

So, what would most plausibly account for the tremendous growth in BankAmerica's OTC derivatives positions from March 31, 2020 to December 31, 2020? As you know, I follow the COT reports quite closely and nothing in those reports or the Bank Participation reports offer me much of a clue to explain the explosion in BankAmerica's OTC position. But when I started to contemplate the unusual developments during the nine months from the end of March 2020 thru yearend, I think it dawned on me.

The unusual developments over the nine months in question certainly included the silver price blast to the downside, when silver fell from over \$18 to under \$12 (a ten-year low) in a matter of days and in which JPMorgan was able to completely eliminate and buy back its short position in COMEX silver (and gold). But that wouldn't account for the massive increase in BankAmerica's OTC derivatives position from March 31 to Dec 31, 2020.

Then it dawned on me – the other highly unusual development of 2020, aside from the price action in silver and gold, was the unprecedented and shocking increase in silver and gold physical holdings. In silver, there was much more of an increase in ETF holdings, mainly in SLV, but also in other silver ETFs; whereas in gold, there was much more of an increase in the COMEX warehouse inventories (although there were substantial increases in GLD and other gold ETFs). Close to 300 million oz came into the silver ETFs, starting around April 1 into the summer.

If you'll recall, in trying to explain where the physical silver was coming from at the time, I first opined that it was coming from JPMorgan in the form of a lease to other banks, before then suggesting later that perhaps JPM had reached some type of regulatory settlement with the CFTC and Justice Department in which JPMorgan disposed of 300 million oz in exchange for not being put out of business. After a short while, I flipped back to my original lease premise, after considering that JPM was not about to part with that much silver at then-current prices under any conditions – certainly not due to pressure from the DOJ or CFTC (maybe the Kremlin, but no US authorities).

The documentation in the OCC reports does point to my leasing premise. After all, at the prices at yearend (\$26.50), \$8.3 billion worth of precious metals derivatives would come to just over 300 million oz. I would imagine such a lease would have to be reported somewhere and the OCC derivatives report is the most logical place. As to why BankAmerica (if I'm fitting the pieces into the puzzle correctly) would borrow that much silver with the obligation of returning same at some later date and price, you'd have to ask them. But I would remind you that financial history, whether over the last week or so (think Archegos Capital) or since banks have existed is a never-ending story of massive miscalculations – so why not?

As to why BankAmerica would engage in such an apparently foolhardy venture of borrowing 300 million oz of physical silver with the promise of having to return it someday, you have to first

understand the nuttiness of precious metals leasing to begin with. Someone with the physical silver (JPMorgan in this case) relinquishes the metal to an institution (BankAmerica) promising the metals return someday. Aside from the promise of the physical return of the metal, JPMorgan also gets an undisclosed rental income. BankAmerica, not wishing to simply hold the metal because there's no real purpose in doing so, turns around and sells the metal to a completely independent third party, in this case the silver ETFs, who's investors pay cash money for the free and clear title to the metal. BankAmerica gets the full use of the cash (\$8.3 billion) to do with as it pleases.

If silver goes down in price or stays the same, no big deal for BankAmerica, provided it can buy the physical silver back on the open market whenever it decides. However, if silver prices rise sharply and if it's not so easy to buy back 300 million physical ounces (like now), BankAmerica is up the proverbial creek without a paddle – just like the nitwits at Barrick Gold and AngloGold were 20 years ago when the time came due for them to pay back the gold they had leased. History may not completely repeat itself, it is written, but it sure does rhyme.

In effect, if BankAmerica did borrow and sell the metal to the silver ETFs, as appears to be the case, it is now short 300 million oz of physical silver, which is a heck of lot worse than being short 60,000 contracts of COMEX silver futures. The only way these people could sleep at night is by not being remotely aware of the full dimensions of this transaction – just like Barrick and AngloGold were unaware until it was too late.

Lastly and most importantly, if I've put this new piece into the puzzle correctly, the fact that 300 million ounces of physical silver was borrowed last year that found its way into the silver ETFs (plus what I would estimate is another 100 million+ oz since the start of the New Year) shows how tight the wholesale physical silver market is because that much silver could never have been bought in the open market without having launched the price to the heavens.

At the time when all this silver was flowing into SLV and other silver ETFs last spring, the outward appearance was that it was being sold and bought by market participants engaged in legitimate free market transactions. However, if one side, the sellers, were simply dumping metal on the market it had borrowed and now have little hope of returning, well that's something quite different. What's "different" is that metals leasing for the purpose of dumping and suppressing prices is as anti-free market and manipulative as it gets.

And where the heck is the CFTC, SEC, and now the US Treasury Department (OCC) in all this? These are the frontline regulators reporting the data, either in the COT reports, public earnings reports by the companies involved and now in the Quarterly Derivatives reports that show or reasonably suggest something is definitely amiss in silver. Yet trying to get reasonable explanations to what the data actually mean is like trying to pull teeth without anesthesia. Needless to say, it shouldn't be that way.

Turning to other matters, every day that goes by is another day closer to when the CFTC will respond to the questions I raised in my March 5 letter. Those questions, of course, revolved around the Commission explaining how the price of silver wouldn't have truly exploded into Feb 1 had not the 4 biggest shorts on the COMEX added more than 33 million oz of new short sales on the price bump? As a reminder, the 4 big shorts were the only short sellers that reporting week. I also expect a response to my question to the Commission explaining how the concentrated short position in COMEX silver, which is and has been the largest such short position of any commodity in real world production terms, wouldn't suppress the price of silver.

Another question that I've asked previously is for the Commission to explain why the 4 big shorts have never bought back silver short positions on higher prices, but only when silver prices fall? Are they magical traders or is there some secret law mandating they never buy back shorts on higher prices?

I know these are not easy questions for the Commission (or anyone) to answer in straight-forward legitimate terms, but they need to be answered if the Commission expects the growing grassroots movement surrounding silver to go away. More importantly, the agency should be seeking to reassure the public that everything is on the up and up in silver, not a sentiment that currently exists, as far as I can tell.

And please know that I believe I understand the seriousness of the issue and how the Commission must be careful in what it says, because it is likely to influence the price. The only question is if the Commission (and the individual commissioners) chooses to stick with its former take that all's well with the concentrated short position in COMEX silver, meaning there's nothing wrong with price suppression – or if it finally stands up and asserts that there is some legitimacy to the allegations of price suppression through the concentrated short position. Yes, I admit to trying to make it the black or white issue that it is.

As far as what to expect in Friday's Commitments of Traders (COT) report, the simple answer is that I'm not sure. Both silver and gold prices were higher over the 4-day reporting week ended yesterday, silver by more than a dollar and gold by more than \$55, almost always the prescription for non-commercial buying and commercial selling. Silver did close back above its 200-day moving average, further adding to suggestions of non-commercial buying and commercial selling. But trading volumes were low and changes in total open interest for both gold and silver for the reporting week were negligible, although there was a pretty big one-day jump in gold yesterday.

I suppose I would imagine some moderate non-commercial buying and commercial selling in silver, but am less sure in gold, because it is still so far below all its key moving averages and because there have been times in the past when gold (or silver) has rallied but remained below key moving averages where the managed money traders have added to short positions on rallies that remained below the moving averages. I guess I should leave it at not knowing what to expect in gold. However, please don't interpret that as me backtracking at all from my take that the market structure in both silver and gold is super-bullish and that whatever this week's report shows, the set up is for an explosive rise.

As far as how the 8 big shorts are faring financially, at publication time they are further in the hole from Friday's close by roughly \$300 million, putting their total losses from June 2019 at \$9.3 billion.

Ted Butler

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Silver – \$25.25 (200 day ma – \$24.84, 50 day ma – \$26.29, 100 day ma – \$25.67)

Gold – \$1742 (200 day ma – \$1859, 50 day ma – \$1767, 100 day ma – \$1814)

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