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## February 26, 2020 – Bear Stearns Deja vu?

Having traded as high as \$1691 in COMEX April gold and \$18.92 in March silver on Monday on near-record volume and closing not far from those levels as of the 1:30 PM EST settlements, prices sold off sharply in the always thinly-traded afterhours. As expected, the all too common occurrence drew complaints of market rigging. To be sure, the sudden selloff was deeply suspicious, but the suspected culprits were not surprising when one examines the known data. Those long had nothing to gain by driving prices sharply lower when trading liquidity was at its lowest. The only entities that stood to gain by the sudden selloff were those most short – aka the 7 biggest short sellers.

At Monday's price highs, the 7 big shorts in COMEX gold and silver futures were in the hole by another one billion dollars, pushing their total combined open loss to a record \$8.2 billion. The selloff that started at 2:30 PM EST and continued through Tuesday morning, allowed the big shorts to wipe out the additional billion dollar impairment and left them at Friday's then-record \$7.2 billion underwater mark. If one is looking to understand what makes gold and silver prices tick, it's wise to look at those who have the most to gain or lose. That's why I monitor the financial scoreboard of the 7 biggest shorts. (As always, I'll update the big 7's financial standing when I send this article later).

All derivatives positions, both long and short, are open positions that must ultimately be closed out at some point. Futures positions can be rolled over almost indefinitely, as opposed to options positions which are terminated on specific dates. Since futures positions can remain open (by roll over), both the longs and shorts must deposit additional margin money when positions move against them, thus assuring the integrity of the contract. That's another reason why I monitor the financial scoreboard of the 7 big shorts.

Actually computing the financial standing of the 7 big shorts in COMEX gold and silver is rather simple. I just take the weekly net concentrated short positions of the 8 largest traders in COMEX gold and silver futures and subtract JPMorgan's short position (since it holds massive physical gold and silver stockpiles and the other big shorts do not). As of the most recent COT report, the 7 big gold shorts held 280,000 net COMEX contracts (28 million oz) and 90,000 COMEX silver contracts (450 million oz) short. Therefore, every dollar move in gold means \$28 million to the 7 big shorts and every 10 cents in silver means \$45 million in gain or loss.

While it's true that the 7 big shorts have never collectively bought back short positions on higher prices and at a loss, it's not written in the Bible or the Constitution that someday they won't be forced to do so. If the big shorts ever do buy back short positions on higher prices, in addition to being the first time such a circumstance has ever occurred, it will dictate a sea change from how gold and silver prices have been determined for nearly 40 years.

Let me be clear in what I am saying – I can't know when the big shorts will collectively buy back short positions on higher gold and silver prices for the very first time, but as and when they do buy back on higher prices, then prices will behave differently than anyone has ever witnessed. The only reason silver, in particular, is as cheap as it is – is because the big shorts' position has depressed prices. Without this short price cap, silver would be much higher.

The only possible alternative is that we do experience a sharp selloff in which the big shorts, once again, buy back short positions on lower prices and then refrain from adding new shorts when prices begin to rally. I've held this alternative view for quite some time, but it's starting to look like even if we do get a sharp selloff, the big shorts have dug themselves into such a deep enough hole that it's hard seeing them buying back short positions without incurring steep realized losses, which would also be for the very first time.

Since the single most important price factor is whether the 7 big shorts will be able to cap and turn prices lower or will fail and instead rush to cover and set off a discontinuous event to the upside, let's examine the prospects for either outcome as objectively as possible. There can be no doubt that the 7 big shorts are holding, by a wide margin, their largest ever net gold and silver short positions and at the largest open losses ever – more than double the previous largest open losses held in 2016. It is this circumstance that creates, simultaneously, the elements of extreme danger and motivation to the 7 big shorts.

Never have the big shorts been more motivated to rig a selloff and never have they been in such jeopardy should they fail to do so. Simply put, the stakes have never been higher. The last time we were in this position was twelve years ago, when Bear Stearns was the largest short seller in COMEX gold and silver futures and on a rapid journey to self-destruction. Upfront, at that time I had no idea Bear Stearns was the big COMEX gold and silver short seller and would not learn of this until months later. But, as it turns out, the lessons of Bear Stearns' collapse reverberate more loudly each passing day.

It is nothing short of astounding that more don't point that Bear Stearns' collapse as being closely connected to its short positions in COMEX gold and silver futures. In early January 2008, Bear Stearns' stock was selling for more than \$90/share. Little more than two months later, it would fail and agree to be taken over by JPMorgan for \$2/share. Over that same time, gold prices soared by \$200 to more than \$1000/oz, the highest level in history and silver rose by \$5 to \$21/oz, its highest price in 30 years. How could the largest short seller not get hurt by that price action?

Do you think it could possibly be just a coincidence that Bear Stearns failed on the very same day (March 17, 2008) that gold and silver hit those record high prices? Or that within days of its takeover by JPMorgan that gold and silver prices would fall by nearly \$100 and \$4 respectively, once the carcass of Bear Stearns was discarded and JPM was running the show?

The most shameful aspect of the Bear Stearns' debacle was that the federal commodities regulator, the CFTC, not only presided over the sordid affair, but then went out of its way to flat out lie to the public about there being no problem with big concentrated shorts in COMEX silver. Huh? The biggest short seller just went out of business on the same day prices hit record highs and the agency in charge lied and pretended all was well. At the very least, a responsible agency would have worked to make sure such a failure would never occur again by instituting the one sure preventive measure to head off a repeat of Bear's failure, namely, by insisting on legitimate position limits. Instead, 12 years later we are presented with proposed limits so high that they would limit no one.

I can't help but resurrect the failure of Bear Stearns to highlight the current plight of the 7 big shorts. In reviewing the COT data from that time, there is not the slightest evidence that Bear made any attempt to buy back its short positions – it just rode the gold and silver price rise out and actually

added new short positions, similar to the behavior of the 7 big shorts today. And, just as the CFTC stood by doing nothing back then, it is doing the same today.

Back in 2008, JPMorgan was called on to take over Bear Stearns, but that option doesn't appear viable today, what with the bank about to be charged with some type of criminal manipulation of gold and silver prices by the Justice Department. Ironically, the bank's woes seem to stem from the dirty market tricks and traders JPMorgan acquired when it took over Bear Stearns. Besides, JPM has already immunized itself from higher gold and silver prices by accumulating physical metal for the past 9 years and it's hard to see how it would benefit from rescuing a big gold and silver short in trouble today.

That's not to say that the 7 big shorts can't rig some type of selloff and must be considered as dangerous as cornered wild animals. For decades, the big shorts have always prevailed in the end, a record thoroughly documented (with the exception of Bear Stearns). In fact, about the only plausible reason to expect another sharp selloff, aside from the desperation on the big shorts, is the fact they have yet to fail and resort to buying back shorts on higher prices.

And I continue to be unfazed by silver's relative weakness compared to gold, chalking it up to the simple fact that silver continues to be the most manipulated market in the world, as evidenced by its concentrated short position being larger than any commodity in terms of actual world production. The fact that the 7 big shorts have been hurt much more on gold than they have on silver is cause for cheer, not dismay. My premise resides on the reasoning that anyone foolish enough to be short massive quantities of gold derivatives is likely to be just as fool hardy to be massively short silver, making it very likely that the 7 big shorts overlap in shorting both gold and silver. If, as and when the big shorts capitulate on gold, they are not likely to hang tough on silver.

All that said, conditions certainly appear different today than they were at the price highs of 2008 or 2011. For the record, gold is higher by 65% of its price high in 2008 and down less than 15% from its all-time highs of 2011. By contrast, silver is lower by more than 10% from its highs of 2008 and down an incredible 65% from its 2011 highs. But it's not just where prices are now compared to where they were back then that catches my attention — it's something very different.

To be frank, I can't dismiss the feeling that it may not be long at all before the big shorts begin to throw in the towel and start to panic and try to cover to the upside. Should that occur, the world of precious metals will be radically different than anything we have experienced, regardless of how long that experience may go back. Quite literally, the operating mechanics of the market will be turned upside down if the big shorts move to indiscriminately buy back shorts on higher prices, instead of patiently waiting to engineer selloffs in which to cover.

In fact, I have trouble not seeing silver as the ultimate asymmetrical trade, meaning that based on what the 7 big shorts may do, the potential upside in silver is completely out of proportion from the potential downside. This is subjective, of course, but I would define the downside potential in silver as little more than 10% or so, say no more than \$2 from current levels. I'm not expecting silver to drop that much, but if the big shorts work their typical manipulative magic, a drop of that much falls within the realm of possibility. Such a drop would take silver decisively below its 50 and 200 day moving averages and send prices back to levels not seen since last summer.

Please remember that the big shorts' real money problem is gold and to climb out from the deep

financial hole the big shorts are in, it is mandatory they smash gold prices, as smashing silver alone won't do them much overall good. In gold, it would take a selloff of around \$250 to penetrate the 50 and 200 day moving averages and take prices back to the levels of last summer. I'm not expecting these selloffs to occur, just outlining the price landscape should a typical cleanout occur. In fact, I'm betting against such a drop. However, if selloffs of such magnitude do take place, let me say way in advance that silver will be the buy of a lifetime. It's just that I think it qualifies as that now.

My point is this - I can't assign precise or accurate odds on whether the big shorts will succeed yet again in rigging gold and silver prices low enough to induce a sufficient number of (mostly) managed money longs to sell and go short or they will fail in that attempt. So let's call it 50 to 50, or even higher odds to the downside.

But while the odds may be a tossup or even more configured for a selloff, there is no comparison between the likely price responses should the big shorts succeed or fail. Complete success by the shorts suggests the downside targets outlined above, while a failure points to an upside price move out of proportion with anything previously experienced. To be specific in silver, a big short failure should translate into an up move of dollars a day for more than a few days. Call it \$2 to the downside, \$50 or \$100 to the upside. If there is a better risk/reward ratio available, I'm not aware of it.

As for what to expect in Friday's Commitments of Traders (COT) report, this reporting week, I'm not sure. In the prior reporting week, a \$30 gain in gold resulted in a massive increase in managed money buying and commercial selling (nearly 48,000 contracts) as total open interest increased by 57,000 contracts. This reporting week, gold ended the week (yesterday) up more than \$45, after being up by as much as \$85, and as total open interest increased by around 18,000 contracts.

I get the feeling that those managed money and other speculators that bought at the price highs may have sold out on the steep decline from Monday's peaks, but that's just a guess. I would imagine increases in managed money buying and commercial selling, but will be most sensitive to what JPMorgan may have done, as well as the 7 big shorts.

In silver, prices ended the reporting week roughly unchanged, after having surged as much as 75 cents at Monday's highs. As was typical (being the most manipulated market), the selloff was much more severe in silver into yesterday and new price lows were achieved this morning. Total open interest was largely unchanged for the reporting week, but roll overs and spread positioning undoubtedly affected total open interest. As was the case in gold, I'm more inclined to examine the data when the COT report is released, rather than speculate on what it will show.

As far as how the 7 big shorts stand as I get set to send this article, while they succeeded in turning prices back sharply from the Monday highs, their relief is much more subdued since Friday's close. Gold prices are actually up a bit from Friday's close, while silver is down about 50 cents or so, granting the big 7 a bit less than \$200 million in relief from Friday's close and leaving their total open and unrealized loss at roughly \$7 billion.

Ted Butler

February 26, 2020

Silver – \$17.95 (200 day ma – \$16.92, 50 day ma – \$17.82)

Gold – \$1649 (200 day ma – \$1474, 50 day ma – \$1555)

**Date Created**

2020/02/26