

July 22, 2020 – The Game Has Changed

Following up from Saturday's comments, it's just my nature not to conclude that recent price action proves that something is 'up' in silver, along the lines as I have outlined them. Of course, the recent price action is certainly in accord with many of my long held premises. But having experienced the full measure of the COMEX silver manipulation for the past three and half decades and, more specifically, the handiwork of the supreme silver crook, JPMorgan, over the past 12 years, I'll need to see more of the price action of the past few days to conclude the manipulation is history. That said, silver is still dirt cheap and could and should only be beginning its price journey higher.

Still, even if it's too early to unfurl the 'mission accomplished' banner (and remaining mindful of what can happen when you do), let me stick to matters that can be spoken of with a higher degree of certainty. One such matter is that the game in silver and gold has changed over the past year or so. The 'game' as I would describe it was the price setting process that existed for the 35 years prior to the change that came over the past year.

The game consisted of paper speculators, called managed money traders, buying and chasing silver and gold prices higher on the COMEX, always to be met with short selling by other speculators, called commercials, until such time as the paper buyers became satiated and began to sell. At that time, the commercial speculators would then grease the price skids to the downside and buy back their short contracts at prices less than sold on average. In doing so, the commercials achieved a perfect trading record of never collectively taking a loss, as verified by concentration data in Commitments of Traders (COT) reports.

While the commercial speculators were given scares at times when silver and gold prices surged higher, even including the demise of the largest short seller at the time (Bear Stearns in 2008), they almost always held ranks and succeeded in eventually prevailing against the managed money traders by rigging prices lower in the end. But more than 35 years of success came to an end, starting last summer. For the first time, after establishing significant short positions in the early summer of 2019, the commercials' unblemished record of collective success stopped working in gold and, later, in silver. Of course, I'm exempting JPMorgan from the 'stopped-working' description as these guys win no matter what the circumstance.

For the past year, I have chronicled the big shorts' failure to rig prices low enough to flush sufficient numbers of managed money traders into selling and it is this failure which is recorded in my running financial scorecard of the big shorts' losses. In essence, this is the game changer and it's hard to see how the genie can now be put back into the bottle.

One never wants to underestimate the treachery of the big shorts (mostly banks), particularly when they become desperate, but having demonstrated that they may not be in control any longer would seem to encourage others to take them on. I've always portrayed the big COMEX shorts as the very few aligned against the rest of the world and over the past few days, at least, the world seems to finally be prevailing. It's important to remember that this is the way it should be (the law of supply and demand) and the only reason it feels so strange is because it has been such a rarity in silver over the past few decades.

In Saturday's "Perfect Solution", I opined that an agreement may have been negotiated between the entities that mattered, namely, the Justice Department, the CFTC, the CME, the most important entity, JPMorgan, and the big shorts. I didn't mean to imply that all the shorts were included and in the review section describing the big stoppers of silver in the July deliveries, I listed four big stoppers on the other side of JPM's 6000 contracts (30 million oz) issued. If there was an agreement, not every short was covered.

The Bonfire of the Option Sellers

One thing that I haven't mentioned in a very long time is that there is an extraordinary amount of call options on various forms of silver, including COMEX futures and on shares of SLV, and even in OTC dealings. As a reminder, call options are derivatives contracts, meaning there is a short for every long in every call option contract, just as there is in futures contracts. (Put options, or bets for lower prices, are not germane to this discussion). While many calls are covered, either by the seller owning the underlying stock or future or by the purchase of other calls in a spread transaction, there are many call buyers who own a variety of straight outright calls, often at strike prices way above the price of silver at the time of purchase. I've referred to these in the past as kamikaze options and they are usually purchased by those deranged enough to believe that silver can suddenly jump higher in leaps and bounds with no apparent reason.

Over the past several years, such call option buying has been a losing affair (as evident in my tax returns, or better yet, just ask my wife what she thinks of options), with the vast majority of out of the money call options expiring worthless. The sellers of such call options have been the distinct winners and I would imagine had grown more confident over time in continuing to sell such options, as nothing succeeds like success. But every once in a while, silver can and has rocketed higher in price and what was a consistent money making experience for the option sellers can suddenly turn into a money losing proposition of hard to imagine proportions.

I bring this up because much of the current surge in the price of silver appears to be related to covering by short option sellers, which represents a whole new level of short covering – separate from any COMEX futures short covering. It is a potential buying force that ignites rarely, but when it does ignite it burns hotter than just about any other type of short covering.

I am increasingly convinced that the surge in silver prices is due to the call option sellers panicking to buy back, under incredible duress, any form of silver to limit their obscenely mounting losses. Under the type of silver price surge witnessed over the past few days, it is not inconceivable, for instance, that a call option worth \$5 or \$10 to suddenly be worth 10, 20 or many times more. Because these are derivatives contracts, the sellers are responsible for immediately coming up with additional cash (margin), which is way out of proportion with what has been experienced for many years.

This is the genesis of the description of call option sellers picking up nickels and dimes in front of an oncoming steamroller. Everything works fine as long as you don't get too close and get rolled over – then everything is as far from fine as can be. By selling naked call options in a depressed market

(or put options in an overvalued market) you can go from making very decent money market returns for long periods of time to sudden bankruptcy. I would be very surprised if we don't soon read of call selling casualties in silver emerging in the near future.

Those call option sellers unable or unwilling to immediately deposit extraordinary amounts of variation margin must buy back the calls sold short or some form of silver that will limit additional losses. There is really no choice as far as the immediacy of coming up with cash or buying back — if the call option seller hesitates in any way, his or her broker will buy the position back for the seller, as it is the broker which is ultimately liable to the central clearing organization. Any broker will tell you that the absolute worst thing that can happen (to a broker) is for a customer to become so impaired as to land in a debit situation — where the brokerage has to go after the customer for money owed.

How much potential call option short covering exists in silver? A lot, although it's hard to quantify as it's not a case of simply looking at total open interest. Many call options are not plain vanilla straight bets; there are all types of spread bets that lessen absolute exposure. Not trying to overstate the exposure, between call options on COMEX futures and call options on SLV, but not including OTC dealings (which are opaque and could be a real wild card), I'd put the total exposure as around 250 million ounces, and much of this exposure may have been covered at the time you read this. Then again, maybe not, as it's hard to speak with precision.

I would make two points. One, the call option sellers' short covering should burn out quickly, but given the panicky urgency of limiting losses first and asking questions later, it's very hard to know the burn out point in terms of price. My second point is that this whole call option short covering is very much a separate bullish layer not usually included in the reasons given for why silver should move much higher in price.

Recent events prompt me to recall a thought held by my dear departed friend and silver mentor, Israel Friedman. Izzy loved silver more than most and developed a particular fondness for American Silver Eagles, although the vast bulk of his silver holdings were in the form of 1000 oz bars, which he acquired through futures delivery and kept stored in the COMEX warehouses. Anyway, one of Izzy's predictions was that someday the US Mint would stop producing Eagles due to a shortage of silver and the premium on the coins would soar.

Due to health reasons, Izzy stopped focusing on silver shortly after prices hit their peak in 2011 and collapsed thereafter and to my knowledge he was unaware of the five years or so, until 2016, that the US Mint cranked out close to 40 million Silver Eagles annually, as well as my contention that it was JPMorgan behind the big buying of Eagles (which it promptly melted into 1000 oz bars to the tune of 150 million oz, when combined with Silver Maple Leafs). The US Mint (part of the Treasury Department) would have to know this and the Justice Department and CFTC could ascertain the accuracy of my allegations in a couple of phone calls, but none have ever denied my claims.

In a very real sense, JPMorgan used the US and Royal Canadian Mints to assist the crooked bank in its acquisition of silver, knowing that the law required the Mint to produce enough Silver Eagles to meet demand, after making sure prices stayed low due to its excessive short selling on the COMEX. Now that physical silver is much tighter, the US Mint is, once again, playing to JPMorgan's wishes by avoiding any unnecessary extra demand by refusing to produce enough Eagles to meet demand, as the law requires. Sure, the Mint has the convenient excuse of the coronavirus, but it's funny how things always seem to play out in the great crook's (JPMorgan's) favor.

Anyway, I can't help but feel that Izzy's prediction is playing out in that there has been a pretty big premium on Silver Eagles and the Mint has simply not been producing enough. Whether the premium ever grows to the levels that Izzy predicted is very much undecided, but there are not that many predictions made by my old friend that haven't come to fruition.

The flow of metal into the silver ETFs continues to astound, as yesterday's 15 million oz deposit into SLV would indicate. I'm not even sure if yesterday's monster deposit was as a result of the equally astounding trading volume yesterday of 80 million shares, the most in years, if not ever. COMEX futures trading volume was also off the charts. Thus, the well-defined flow of metal continues to come into the world's silver ETFs, confirming my friend Carl Loeb's apt description of the SLV and other silver ETFs, as Death Stars, bound to gobble up all the world's silver in time.

A minor quibble on my part have been the sensationalist reports of imminent buying of silver in the Sprott silver ETF, as a result of the filing of a shelf registration for an additional \$1.5 billion in new shares. There was similar filing a number of weeks back by SLV, in which they registered to sell another 500 million shares, effectively doubling the amount of authorized shares. These new shares filings are strictly pro-forma and legalistic in nature and as such don't mean that amount of silver will be bought immediately. What gives the silver ETFs their Death Star nature is that they are, essentially, open ended mutual funds and will continue to buy physical silver as investors demand new shares. After all, there would appear to be a near infinite amount of investment buying power versus a very finite amount of physical metal in the world. The share filings are just an assurance that no artificial limits are set.

Also, I've seen it mentioned recently, as well as over the years, the thought that all the silver going into SLV and the other silver ETFs (as well as in gold) is somehow suspect or not occurring in reality, despite serial numbers, bar weights and hallmarks being published. I don't consider these gripes as being legitimate, but if anyone strongly feels non-existent physical silver is being reported in SLV or any other ETF, then that person should complain to the SEC and other authorities.

As far as the silver not being physically moved into the SLV, on any given day (like yesterday), because the amounts seem too large to explain that's a different matter. Not for a minute do I suspect that 25 truckloads of physical silver were moved into the vaults of SLV yesterday. But the point is that that much silver didn't need to be physically moved. There should be no question that the silver coming into SLV yesterday and over the past 4 months and into other silver ETFs as well has come from JPMorgan (since it is the only one holding that much silver) and the metal needn't be moved at all - just electronically transferred from JPM ownership to ETF ownership. I've always contended that JPMorgan kept the bulk of its 1 billion oz in London, so no real physical movement is or was necessary.

This week's new COT report should shed light on the most important question, namely, did the big shorts (and JPMorgan) add to short positions on the price rise over the past days? While we'll have to wait for Friday's report to be sure, I found it rather encouraging that yesterday's final total open interest data for silver indicated a rather paltry 1500 contract increase on a day of more than 150,000 contracts in total volume and on a \$1.36 (7%) rise in price. In previous times, I would have anticipated an increase in open interest of ten times the reported level. This raises the thought that the big shorts weren't aggressively adding to shorts in silver (he said with a hopeful glint in his eyes)

For the reporting week, total open interest in gold rose 23,000 contracts (11,000 yesterday) as prices rose nearly \$40, including yesterday's \$25+ burst, setting new 8 year highs. That's not much of an increase in total open interest, all things considered, particularly since the new selling may have come at the hands of the raptors which have been adding shorts and not the big shorts. I hope that continues.

In silver, total open interest for the week did rise about 7500 contracts on a price rise of just over \$2. I would imagine there was further selling by the raptors liquidating longs, so I have to imagine there was some new shorting by the big commercial shorts and you know who, but I have my fingers crossed the new shorting wasn't particularly excessive. Undoubtedly, the data will be complicated due to call option short covering via the purchase of futures contracts.

It's a bit surprising there hasn't been any margin increases announced yet by the CME Group given the sudden burst of price volatility, although I'm sure they would prefer to wait for a price decline before raising margins, so as not to put too much additional pressure on the beleaguered shorts. This is what typically happens.

At publication time, there certainly hasn't been any reprieve for the big shorts, regardless of any deal that may have been arranged behind the scenes. Just from the close on Friday, when I pegged the big shorts as being in a record financial hole of \$10.3 billion, the rally thru today has added another \$2.3 billion in losses (or impairment or missed opportunities or whatever one cares to call it), making the losses an astounding \$12.6 billion or more than \$1.5 billion per trader on average. Talk about a game changer.

It has been two weeks since "The Silver Pressure Cooker" in which I envisioned a possible price lid coming off the silver market. In that time, silver has exploded by \$4 or more than 20% in price (while gold has risen by close to 2.5%). We have a long way to go before my definition of the lid truly coming off the price of silver is fulfilled (no new shorting by the big shorts) and undoubtedly, it's way too soon to conclude that this is it. On the other hand, we did explode to multi-year price highs in silver in ten trading days on no real change in supply/demand that I have seen and are now up \$11 or 92% from the JPMorgan-rigged price lows of just four months ago.

Needless to say, the price moves in silver over the past two weeks and well-before that have qualified as strange, to say the least. Despite the strange price movements and what have been well-documented allegations of price manipulation of the most specific kind possible, the regulators at the Justice Department, CFTC and CME Group, to say nothing of the world's most corrupt bank, JPMorgan, have not been able to utter even a word denying the allegations. That's just marvelous.

As far as expected price moves in the short term, I would be prepared to hold onto your hats, as it

promises to be a very volatile price environment ahead, given the sharp rise to date. Regardless, silver is far from expensive on a long term basis at this point and any setbacks should be viewed as buying opportunities.

Ted Butler

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Silver – \$23.00 (200 day ma – \$17.10, 50 day ma – \$18.11)

Gold – \$1865 (200 day ma – \$1615, 50 day ma – \$1758)

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