

October 14, 2020 – The Proper Perspective on Silver

Trying to put things in proper perspective is not necessarily the guaranteed way to success, but it beats depending on pure luck. Of course, attaining the proper perspective is not the easiest thing to do, particularly when the topic is complicated. Such is the case with silver as an investment asset. On the face of it, you wouldn't think silver would be complicated, since it's a basic element and one would think its analysis would be pretty straightforward. But that's not the case.

This point was brought home to me in a recent note from a new subscriber, who commented that I placed too much emphasis on COMEX futures positioning and details in the COT report. To be sure, this is exactly the case, since I'm convinced such considerations are and have been the prime driver of price. But at the same time, it's my responsibility to convey why I believe such positioning is so important to the price of silver, in terms easily understood by all.

No, I'm not suggesting there's much I can do to convey to all readers, new and old, an instant understanding of the COT report, as it is a very complicated data source in which I uncover new things even after decades of intense study. Therefore, in terms of making the details of the COT report easily understood by all – no can do. But there is something I can do in explaining in simple terms why I feel this is so important and the right approach.

The price of just about all investment assets is mostly driven by basic supply/demand fundamentals. Stocks, bonds, and real estate – the main investment assets – are dominated by widespread and direct ownership and the price of each is determined by the purchase and sale of that ownership. In other words, derivatives trading is small relative to the body of each investment asset. I'm not saying HFT computer trading doesn't influence stock prices from time to time, but such trading's influence in bonds and certainly real estate, is much less.

Even in gold, where COMEX futures trading is influential enough to prompt me to allege price manipulation, the body of existing gold in the world, some 6 billion ounces in total and worth close to \$12 trillion, is vastly larger than the current 24 million oz concentrated short position of the 8 largest COMEX traders. In all investment assets – stocks, bonds, real estate and even in gold, the actual amount of each in existence and widely-owned towers over the amount held in derivatives contracts issued on each, particularly in terms of concentrated holdings.

But it's different in silver and that difference has lasted for the 35 years since I first discovered it. In silver, the concentrated short position of the 4 and 8 largest traders is much larger than the comparable short position in any other commodity when compared in terms of real world production totals. And in comparison with gold, the concentrated short position of the 8 largest traders in COMEX silver is 15 to 20 times larger in terms of equivalent world bullion inventory. Undoubtedly, you've heard me mention all this before, but with the aim of putting it into proper perspective, let me try to describe what this means.

What it means is this – in all investment assets, stocks, bonds, real estate and even gold, since everyone is, essentially, positioned on the long side via actual ownership, the strong bias and common interest is for prices to rise over time and this has largely come to fruition. True, at times this upside bias can get overextended, resulting in periodic large selloffs, but that's understandable. But in

silver, it is markedly different, in that while there is a common body of widespread actual investment ownership, there also exists a highly unique derivatives short position, not present in any other asset to the degree it exists in silver.

Therefore, if one seeks to uncover why silver is so relatively undervalued when compared to all other investment assets, certainly including gold where it fell to 5000 year lows earlier this year, one is forced to seek out what it is about silver that makes it different from all other investment assets. What makes silver so different is that it has a narrowly-held, but extremely large short position that doesn't exist in any other investment asset to the extent it exists in silver. This the proper perspective in which to consider silver. Don't fret about not completely comprehending the details in the COT report (although they are available for verification), but know that what makes silver different from all other investment assets is its highly unique concentrated short position.

Whereas the common ownership basis serves as a tailwind for higher prices in other assets, silver's special concentrated short position means that the 8 big COMEX shorts have to work overtime to make sure prices don't rise too much or rise as much as they would if the concentrated short position didn't exist. The big shorts' motivation is simply a matter of financial survival for them because if silver prices were to rise (as they should), the big shorts would suffer massive and potentially ruinous losses. Therefore, the big shorts have little alternative except to try to keep prices from rising and my weekly COT analysis is largely a reflection of how well or poorly they are faring.

One particularly egregious aspect of the concentrated short position in COMEX silver (in gold as well) is that the position is purely speculative, as opposed to being a legitimate hedge. The "natural" legitimate short hedger in silver would be a silver miner looking to lock in prices to ensure a profit margin. As a reminder, commodity futures trading exists for the purpose of allowing legitimate producers and consumers the ability to hedge and reduce price risk.

But there is scant evidence of widespread silver miner hedging on the COMEX and, in fact, publicly-traded mining companies are required to fully disclose all such hedges in quarterly earnings reports (according to FASB). None, to my knowledge, report or engage in such hedging. Silver mining companies are highly reluctant to hedge on the COMEX because shareholders demand upside exposure to higher silver prices. I've yet to uncover an investor in silver mining companies that doesn't expect higher silver prices and who would avoid, like the plague, any miner hedging the price of silver.

So not only is there a uniquely large concentrated short position in COMEX silver (and gold), it is completely speculative as opposed to being a legitimate hedge. In fact, data in the monthly Bank Participation Report indicate clearly that foreign and domestic banks are the big short sellers in COMEX silver (and gold), not mining companies. The CFTC's (and CME Group's) response to this? I'll let you know when there is ever a response.

Since the concentrated short position in COMEX silver has dominated and suppressed prices for more than 35 years, it is only natural to question if it can be extended for much longer. After all, if the 8 big shorts are going to continue the price suppression they have conducted for the past few decades that is something that should be of concern to all silver investors. While predicting the end of the price suppression is different from describing its existence, there have been some recent important changes that suggest the big shorts' reign is on its last legs.

One such change is that the big shorts' financial performance has been abysmal of late. Starting in the summer of 2019 in gold and kicking in this summer in silver, the 8 big shorts have gotten squarely behind the eight ball. They had to resort to a price smash going into the end of the third quarter (Sep 30) to trim losses by up to \$3 billion, but they still ended nearly \$12 billion in the hole from a year earlier. It's important to recognize that these 8 big shorts, prior to recently had never taken a loss when shorting COMEX gold or silver. What a difference a year makes.

Another important change since mid-March of this year, when silver bottomed at just under \$12 and gold at \$1460, is that JPMorgan has largely abandoned the short side, potentially leaving the 8 big shorts high and dry and at risk for an epic double cross. Prior to this, JPMorgan had been the largest COMEX short seller since the time it took over Bear Stearns in early 2008. Having acquired 700 million oz of physical silver and 25 million oz of physical gold (at a minimum) and fresh into a deferred criminal prosecution agreement with the Justice Department, JPMorgan would seem to have every incentive for avoiding its past leading role in the manipulation of silver and gold prices by shorting aggressively in the future. But as they say, time will tell. However, to date, JPMorgan is ahead by more than \$20 billion on its physical gold and silver holdings, while the 8 big shorts are many billions in the hole and if that isn't a double cross, I don't know what is.

In addition, there have been some genuinely remarkable changes in physical silver and gold that seem directly related to the 8 big shorts and JPMorgan, including record flows of metal into ETFs and the COMEX warehouses. In fact, it's hard to come up with reasons away from the concentrated short position that explain the massive physical flows and record deliveries on COMEX futures contracts. But let me add one more change in silver that I haven't mentioned until now that might aid in putting all this into proper perspective.

When I discovered the reason for the silver price suppression 35 years ago and embarked on a mission to end it by pointing out the concentrated short position on the COMEX, I wouldn't say that I was virtually alone in my public proclamations about the investment case for silver being extremely bullish, but back then the bears were also out in force.

In fact, I remember one such pundit (sadly, since deceased at a young age) who proclaimed at \$4, that he was ultra-bearish and buying put options on silver and how there were more ounces of silver in the world than there were cockroaches. Having grown up in a five story walk up tenement in NYC (with a garbage dumbwaiter in the apartment), I knew firsthand how many roaches could exist in the world and that there was no way that more ounces of silver could possibly exist. Another pundit (still with us) proclaimed back then that if silver ever got as high as \$8 or \$9, there would be non-stop daily boatloads of silver from India due to the high price. Instead, India has been a net importer of silver for 40 years.

Comparing back then (20 years ago and longer) to today, the collective opinion landscape has changed dramatically. Commentators of every stripe (fundamental and technical), particularly among those who formerly focused primarily on gold, have come to project truly astonishing high price levels for silver. If you really scour the universe of commentators, you might be able to scratch up one or two who are bearish on silver, but always for reasons that make little sense. I'm aware of the contrary nature of universal bullishness or bearishness, but this is not the case here, I believe because I'm talking about collective commentary; there can be no question that the investing public is not collectively positioned in silver.

Even in the stock market (and real estate) you can find vocal and well-stated cases made for dramatic declines in price given the historically high prices – not everyone is bullish. I'll leave out what I think will occur, as my point is simply that there is reasonable debate on either side about whether stock (or bond) and real estate prices will continue to increase or decline. That's not the case in silver.

Instead, I think this near universal bullish opinion for silver reflects something stunningly obvious, namely, that silver is way too cheap relative to every other investment asset, including gold. The reason everyone is now bullish on silver is because there is an intuitive recognition that it is just too darn cheap given the facts around it and comparing it to everything else. And I would whole-heartedly agree with this near universal recognition. The only thing missing is the universal recognition for the reason silver is so darn cheap to begin with. But the longer silver remains as cheap as it is currently, the more likely it is that those who are bullish will seek to understand the reason why it remains so cheap.

Here we come full circle. The one and only reason why silver is so cheap is due to the concentrated short position of the 4 and 8 largest traders on the COMEX, just as I have maintained for 35 years. For all this time I have sought and solicited an alternative explanation for why silver is so cheap and I do so again today. But by this time, I believe if there were a better explanation, it would have surfaced. Instead, it is more glaringly obvious than ever that 8 crooked and manipulative large derivatives traders, mostly banks, have aligned themselves against, quite literally, the rest of the world.

Certainly, every mining company producing silver, as well, as every investor in silver or silver mining companies desires higher prices – the same as with every other investment asset. Even the industrial silver users are not unified against higher prices, since so little silver is used per application that any price increases can easily be passed along. There is only one specific segment constantly fighting any price rise in silver as if their financial lives depended on it – the 4 and 8 concentrated short sellers on the COMEX.

It might be different if the 8 big silver shorts had a legitimate justification for being so heavily short COMEX silver futures, lately around 350 million oz. If, for instance, the 8 big shorts were mining companies hedging their silver production, perhaps I couldn't complain. But the average short position for each of the 4 biggest shorts is nearly 63 million oz and there are no silver mining companies that produce that much silver in a year. Besides, the last time (some 20 years ago) that mining companies sold forward against production it ended in disaster – just ask Barrick Gold or AngloGold Ashanti.

Perhaps one good way to consider the effect of the concentrated short position on the price of silver is

to imagine the price landscape if it didn't exist. To be sure, we would still likely have the price volatility created by mindless computer to computer day trading, but I'm convinced that without the guiding hand of the 8 big shorts, the volatility would occur from a much higher price level. There is only one way to know for sure and that would be by observing the level of silver prices as and when the concentrated short position in silver is in line with that of most commodities.

What would the concentrated short position of the 8 largest traders have to be in order for it to be in line with the average such short position in other commodities? Roughly two-thirds lower than it is currently or something close to 24,000 contracts (120 million oz), as opposed to the current 71,000 contracts (355 million oz). It doesn't really matter what the total open interest may be, as long as the concentrated portion is not out of line with every other commodity, as is the case in silver now.

And for those who might point out that the concentrated long position in COMEX silver future is also high, although not as high as the short position, I would reply that the long position is only as large as it is because silver is so cheap. When silver is more correctly priced (much higher), there won't be a large concentrated long position. More to the point is that it does make sense that there would be a large concentrated long position in silver, precisely because the price is artificially suppressed. There is no legitimate argument for a large concentrated short position at current super-low prices — only illegitimate arguments.

I believe the forces are converging to end the illegitimate concentrated short position in COMEX silver futures, as I described above. But in the interim, seeing as I also believe this short position is what determines the current price, I have no choice in continuing to focus on it, even if the detailed discussion of the COT report gets too deep in the weeds and wonky at times.

Another subscriber asked an equally reasonable question, namely, why I don't focus more on changes in the US Dollar Index and general economic developments, such as progress on the stimulus debates (as every other commentator seems to do). As far as the dollar index, it's clear that there is a correlation recently where dollar index weakness matches up with precious metals strength and vice versa. However, there have been just as many time periods where no such correlation has existed. More importantly, I don't see a causal relationship between the dollar index and the metals.

If one wants to argue that a loss of purchasing power of the dollar (the rate of inflation) has a general impact on prices, both for precious metals and other items, then I wouldn't disagree. But a dollar collapse in regards to the US Dollar Index means that the dollar would decline sharply against a basket of other currencies, principally the Euro and Japanese Yen. I honestly don't know the fundamentals that drive currencies and am not sure that many do. If I thought that changes in the US Dollar Index were the principle driver of silver prices, I would say so.

Instead, I'm much more convinced that changes in the price of gold and silver, brought about by trading activities and positioning on the COMEX, drive changes in the dollar index and not the other way around. At times like now, where a strong correlation is obvious, who can really say for sure which is driving the other? It's like the question of which came first — the chicken or the egg? If I thought that changes in the dollar index determined silver and gold prices, I'd assert that, but that's not the case, as I feel it's the other way around. Regardless, if silver and gold prices race higher, I would imagine the dollar index would sell off sharply — just not for the reasons that many seem to assume.

Yesterday (Tuesday) silver and gold prices got smashed, essentially erasing the gains of last week (achieved largely on Friday). While I do believe mindless algo computer to computer day trading was largely responsible for the smash, I can't help but also believe this and other similar selloffs were also aided and abetted by the 8 big shorts. After all, every silver and gold investor, physical metal and mining company investors, included as well as paper long, basically lost, while the biggest winners were the 8 big shorts — same as always.

Of course, the physical metal fundamentals didn't change (except perhaps to attain better value given the lower prices) and the market structure should have improved on the lower prices. Speaking of silver fundamentals, there were a couple of stories on growing solar energy production, including a research report by Goldman Sachs (no link available) which concluded that silver should rise from \$24 to \$30, all things being equal, on increased solar panel demand. A second story on Reuters involved a report from the International Energy Agency that concluded, among other things, that the amount of electricity produced by renewables would overtake the amount produced by coal-fired plants by 2025, with solar becoming the new king of the world's electricity markets, according to its chairman.

<https://www.reuters.com/article/us-iea-energy-renewables/solar-the-new-king-of-electricity-as-renewables-make-up-bigger-slice-of-supply-iea-idUSKBN26Y0E7>

In other news, there was a 4.6 million oz deposit yesterday into SLV, the big silver ETF, bringing the total amount of silver in that trust to more than 563 million oz, which is about 16 million oz shy of the record in early August. Normally, I save commentary on EFT deposits/withdrawals for the weekly review, but I am mentioning yesterday's deposit because it seemed related to the sharp price rise on Friday, best I can determine. If that is the case, then I feel it is noteworthy as it would represent a delay in the deposit — an indicator of potential tightness in the wholesale physical market.

As far as what positioning changes might be in store for this Friday's new COT report, the high-volume price smash yesterday (the day of the report's cutoff) would seem to negate any managed money buying and commercial selling on last Friday's price pop. Thus, I wouldn't expect truly significant positioning changes, given the generally washed out (and bullish) market structures in both COMEX gold and silver.

Of course, I'll be interested in what, if anything, the other big reporting traders may have been up to. Particularly in gold, the positioning highlight has been evolving into the big other traders (who are those guys?) versus the 8 big shorts — not something seen to this point. So, in addition to the 8 big shorts being almost single-handedly aligned against the rest of the world, it would appear a new and separate force is taking on the 8 big crooks. I'm sure I don't have to tell you which side I'm pulling for.

As far as how the 8 big shorts fared financially since Friday's close, the sharp selloff yesterday worked to their advantage. As I get ready to send this out, based upon current prices, the 8 big shorts recovered nearly \$1 billion from Friday's close, leaving them \$13.4 billion worse off as a result of holding short positions from June 2019.

Ted Butler

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Silver – \$24.40 (200 day ma – \$19.60, 50 day ma – \$26.16)

Gold – \$1907 (200 day ma – \$1751, 50 day ma – \$1946)

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