

## January 8, 2020 – What Matters Most

Including today, it has now been only five business days since the end of 2019; not a terribly long time. That's just five work days for the CFO's and top treasury and risk officials at the 7 to 10 largest shorts in COMEX gold and silver futures (obviously, excluding JPMorgan) to ponder what to do about the record large mark-to-market losses booked at the end of last year. On Dec 31, the 7 biggest shorts in gold and silver booked a marked to market loss of \$3.8 billion, or just over \$540 million per trader on average.

While the big shorts have been underwater on their concentrated short positions since the summer, they were able to rig gold and silver prices sharply lower into the end of the third quarter, Sep 30, when the open losses were reduced to around \$2 billion, not good but a heck of lot better than the more than \$5 billion they were out at the price highs of early September. From September 30, gold and silver prices were fairly contained, with gold kept below \$1480 and silver at or below \$17 until December 23, when each staged a five trading day rally to around \$1525 and \$18 respectively that resulted in the open loss growing to \$3.8 billion at yearend.

Worse for the top financial managers at the 7 largest shorts (mostly banks and financial firms, both foreign and domestic), is that the New Year has added to those open losses to the tune of an additional \$1.6 billion through yesterday's close; making the total open loss \$5.4 billion, or more than \$750 million per trader on average as of yesterday (I'll update the open loss when I send this article out later today). A hundred million dollars here and a billion there, and pretty soon you're talking real money. And make no mistake, while these are open, rather than closed-out and realized losses, they are real enough to the organizations involved, in terms of the keeping of books and the advancement of additional collateral (margin) to the central clearing house at the CME Group.

On a collective basis, the open losses to date would already rank in the annals of the largest and most infamous derivatives debacles in history; from Barings Bank (Nikkei futures) and Long term Capital Management (interest rate and equity derivatives) to Amaranth Advisors (natural gas futures) to JPMorgan (credit default swaps). To be sure, the \$5 billion+ open and as yet unrealized loss to the largest COMEX gold and silver shorts is shared collectively by 7 different entities, whereas the most infamous losses in history were taken by individual companies; but my point concerns the relative size of past debacles and the one perhaps in the making in gold and silver.

[https://en.wikipedia.org/wiki/List\\_of\\_trading\\_losses](https://en.wikipedia.org/wiki/List_of_trading_losses)

But there is another very big difference, of course, in that all those prior examples were for closed-out trades, whereas the current situation in COMEX gold and silver futures is very much an open derivatives position yet to be closed out. It could turn out that the big shorts succeed in engineering sharp price declines in gold and silver and in closing out their big shorts at no loss or even a profit. That has always occurred on previous occasions of big concentrated short positions in COMEX gold and silver futures. Then again, it is possible the big shorts won't succeed in closing out their short positions at lower prices, but only at current or even higher prices. At this point, no one can know for sure which it will be – that's the difference between closed out and open positions.

Lots of things are said to influence the price of gold and silver, including surprise assassinations, last

night's missile attacks and other geopolitical developments, interest and currency rates, stock market volatility and more macroeconomic factors that can be recounted here – all in addition to basic supply and demand fundamentals. No doubt all these factors exert some immediate influence on price, but for me (as I believe readers would attest), it all has to do with COMEX futures positioning. The reason I'm so intent on the state of the large open losses confronting the biggest shorts on the COMEX is that I believe the resolution of the open short position will determine future prices more than all other factors.

Back to the plight of the top financial and risk officials at the 7 big COMEX gold and silver shorts. I believe the six day rally into the end of 2019 and the five trading day rally of the New Year and the open losses the rally created, should have resulted in the transfer of control of the big short positions from the traders who established the positions originally to more senior officials at the institutions involved. The traders responsible for establishing the large short positions are typically young, aggressive and short term oriented. They trade on behalf of the institutions they work for, seeking gains that will result in bonuses and increased compensation. Should these traders incur large losses, they stand to lose bonuses and perhaps even get terminated, but since they are trading with the institutions' capital, the losses are borne by the institutions, not the traders personally.

The senior treasury and risk officials at the institutions, on the other hand, are responsible for safeguarding the capital position of the institutions. In a real sense, these officials are the adults watching over the children (the traders). For more than 35 years, the senior officials haven't had to scold or reprimand the traders much, since the traders never collectively incurred actual losses in trading COMEX gold and silver futures from the short side. The traders and the institutions did have to endure periods of time when the short positions moved against them, resulting in open losses and having to come up with increased margin; but in the end, the traders were always able to rig prices lower and close out what were big open losses with no actual realized loss. Everything always ended up hunky dory when the dust settled.

What I just described was the experience of the past 35 years in which gold and particularly silver were, in essence, manipulated in price. The speculators, mostly the managed money traders, would buy large numbers of futures contracts causing price rallies which were sold short into by the traders at the big commercial institution. The short sellers knew that there was a limit to how many contracts the managed money traders could buy and they also knew that when the managed money traders were done buying, they would have to sell and the commercial short sellers would then buyback their shorts at lower prices and at profits (or no losses).

This is the repetitive wash, rinse, repeat cycle of futures positioning that has dominated gold and silver prices for three and a half decades and to which there is now near universal recognition and acceptance in the form of the Commitments of Traders (COT) report. But as regular and reliable as the COT report has been in explaining price moves, the positioning was inherently corrupt and manipulative because the big commercial shorts were engaged in a game not related to anything but taking money away from the highly mechanical managed money traders. In other words, changes in gold and silver prices had nothing to do with anything but the big commercials cheating the managed money traders any way possible.

Now, however, there are signs that the big commercial shorts' control over the crooked COMEX game may be coming to an end. Chief among these signs is the recent financial experience of record

open losses in a remarkably short period of time. For some reason, over the past few months the managed money traders which would have always sold aggressively in the past in response to the downward moving average penetrations in the fourth quarter failed to do so. Without that expected selling, the big commercial shorts have been unable to buy back their short positions (or unwilling to buy back at prices which would result in realized losses).

Looming over the whole circumstance is the remarkable positioning of JPMorgan, which has parlayed its role of principal COMEX short seller to what appears to be an increasingly minor role on the short side. Far more important, however, is that JPMorgan has used the low prices that it was instrumental in creating to accumulate since 2011 massive amounts of physical gold and silver – by my count, at least 900 million oz of silver and more than 25 million oz of gold. As has been true for quite some time, when gold and silver do get set free, JPMorgan will be the biggest beneficiary, regardless of whatever it may hold short on the COMEX.

In the short term, I sense that it will be the actions (or lack thereof), of those senior officials at the big COMEX shorts that will determine price direction. Because the financial pressure has intensified so greatly over such a short period of time (11 trading days from December 23 through today), I may be too quick in anticipating how and when the senior officials will react. I don't expect the big shorts to simply roll over and give up without a fight and that translates into the potential for sharp selloffs (which is occurring as I write this).

In a market rigged, basically, by a handful of large concentrated shorts for more than 35 years, now that the shorts' backs appear to be up against a wall, I don't expect them to go quietly into the night. In fact, going quietly is impossible due to the reality of the situation. Either the big shorts will succeed in truly smashing gold and silver prices sharply lower AND inducing the managed money traders to sell at much lower prices or they will fail to do so. Remember, both the rigging of prices lower and the aggressive sale of contracts by the managed money traders are required for the big shorts to get off the hook.

I would ask you to take a moment to consider the scope and consequences of what would occur should the big shorts fail to rig prices lower and buy back their massive gold and silver short positions. This is the vision that occurred to me more than 35 years ago, yet has failed to materialize through today. Despite that failure to materialize, I remain undeterred. This is something that must occur at some point, even if I am incapable of predicting precisely when it will occur. And in all the time I have studied silver, never has it looked more likely that the time of resolution may be at hand.

Put yourself in the place of the senior officials at the institutions holding the big gold and silver shorts. Over just the past two weeks, you have come to learn that the young traders who assured you that things were under control were not only wrong, but have achieved the largest quarterly and year end mark-to-market loss in history; and the losses have increased in the New Year by amounts never contemplated. Were you to be in their place, would you not completely disregard and mistrust any further assurances by the traders that all will turn out well in the end and instead look to safeguard your own and the organization's continued financial viability? Of course you would, as it would be what any reasonable person would do. No one wants to end up on the list of largest derivatives losses.

Now take it one step further and picture what you would do, if you were in the shoes of a senior official who wanted to make sure your current extremely troubling predicament was not a continuing nightmare. Yes, you would seek to eliminate any possibility of a recurrence and the only way to do that

would be to order the short positions closed out. And if those senior officials which are actually experiencing the nightmare of record open losses aren't close to ordering all gold and silver shorts being closed out, then I don't know how they achieved their current positions in the first place.

The whole point of this exercise is for you to picture what a decision to close out open gold and silver short positions would result in. Such an order would turn the gold and silver world on its head. After all, the only reason gold and especially silver prices have been as cheap as they've been is because of the excessive and concentrated short selling by a relative handful of large entities. Remove that short selling and there would be no reason for prices not to explode. In essence, the big short sellers, should they cease to sell short would remove the only selling force of consequence.

But wait a minute I'm not just talking about selling pressure suddenly being removed, it's much more than that. Precisely because the large concentrated short position is an open derivatives position, it's not simply a case of no more selling and walking away I the short position must be bought back in order for it to be closed out. The moment there is an attempt to close out the massive concentrated short position, that's just another way of saying a massive buy order will come into the market. And not just a massive buy order, a massive buy order from what were the biggest former sellers. Mechanically, this would create a selling vacuum in which prices would have to explode.

I'm not saying all the senior officials at the institutions which are short will simultaneously order the closing out of all short positions, but because the short position is so concentrated (meaning it is held by relatively few entities) any move by even one or two of the big shorts to buyback and close out short positions would automatically put tremendous pressure on the remaining shorts to do the same. The closest example I can offer is that it would be like spontaneous combustion I the sudden explosion of a buying force that feeds on itself until it burns out. The fact is that the 'oily rags' about to combust are set out in the positioning data in the COT report and price action to date. None of this is a figment of my imagination.

And here's another thought I can't shake. If, in fact, any of the senior managers at the big shorts do order the short positions closed out, that's a decision that can and will be made at any time and without advanced prior notice. As I've stated, most of the big losses have occurred over just the past two weeks and at the time of the year when holiday observance generally results in key personnel being away from the office. To me, that suggests an even more sudden reaction, if, as and when it occurs.

Please keep in mind that none of this has anything to do with what is normally associated with gold and silver price movement. This whole circumstance, namely, the possibility that the big shorts are about to abandon the game that has controlled and manipulated gold and silver prices for decades is not in the least priced into the market. But not only is it a black swan that few have any sense of, it is a factor, to my mind, that so vastly overshadows all the other factors related to gold and silver that it is the only thing that truly matters.

Of course, it would be really special to be able to get some advanced warning that all this was about to go down, but the nature of the beast argues against that. If it does happens, it happens in a flash without warning. Still, I'd be lying if I said I wasn't on the lookout for signs that one or more of the big shorts were starting to cover. The only two signs I can imagine would be price action itself, which almost by definition would be too late to capitalize on. The only other way would be in the COT report itself; but even there, such confirmation may be too late, given the publication schedule.

That leaves daily observation of price, volume and changes in total open interest. Up until the past couple of days, I can't say I've seen many signs of attempted short covering by the big concentrated shorts. If anything, the big shorts seem to have added more shorts, as was the case in Monday's COT report. But my antennae may have sensed a change in the force field the past couple of days. Trading volumes have been absolutely enormous, up to and including the volatile trading resulting from the missile attack last night. If one needs to cover large positions, as the big shorts need to do, extremely high trading volume and price volatility would be basic requirements, at least by an individual large short or two.

Plus I've also noticed that total open interest has dropped over the past couple of days in gold, which strikes me as odd in that we are in the prime period of switching and rolling over from the lead February COMEX gold contract. I still don't know why so many new spreads and therefore, total open interest has been created at this time of the month, but I am now suspicious that total open interest, by not increasing sharply these past two days as has been typical, may be camouflaging a true reduction in the concentrated short position. In any event, I'm not at all confident of what to expect in Friday's COT report, but will be prepared for just about anything.

The big price smash from the new highs witnessed last night has taken some, but not much pressure off the big shorts. At publication time, today's sharp price drops in gold and silver have erased the open losses created by the price jumps on Monday and Tuesday, putting us back to unchanged from Friday and leaving the 7 big shorts' total open losses in COMEX gold and silver combined at \$4.9 billion. That's still up from the \$3.8 billion mark-to-market loss of 12/31, as I'm sure any of the senior managers at the 7 big shorts would attest.

Ted Butler

January 8, 2020

Silver – \$18.10 (200 day ma – \$16.44, 50 day ma – \$17.34)

Gold – \$1555 (200 day ma – \$1427, 50 day ma – \$1488)

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