July 20, 2022 – The New Moment of Truth

More than 35 years ago (where did the time go?), a regular feature of my intense daily discussions with my now-departed friend and silver mentor, Izzy Friedman, was the approaching moment of truth for silver; when demand for physical silver would suddenly exceed the ability of the short sellers on the COMEX to deliver the amount demanded. At that time, the years of price suppression would suddenly be exposed and the price of silver would soar.

Over the past few decades, the coming prospective inability of the silver short sellers to meet physical delivery obligations has become increasingly popular and many have taken to following, in great detail, the daily statistics published on COMEX deliveries and warehouse inventories â?? something I admit to never having missed a day of for decades. Certainly, thereâ??s great logic in studying the daily statistics from the COMEX, since the exchange is the largest precious metals exchange in the world and the holdings in its approved silver warehouses constitute the second largest stockpile of metal in the world (after SLV).

However, while I would never completely disregard the possibility of a silver delivery default on the COMEX â?? particularly after the default in LME nickel four months ago â?? Iâ??ve come to embrace a different coming moment of truth for silver. So significant, even financial system-shattering, would a delivery or short default of any kind be in COMEX silver, particularly with so many expecting it, that it dawned on me that it is most unlikely to occur. It would just be too obvious and pat for a default to occur in COMEX silver with so many expecting it.

Surely, a default in COMEX silver would be in such full view that its repercussions would be felt far and wide. Perhaps the greatest scrutiny would be placed on the regulators (the CFTC, DOJ and the CME Group), given the widespread attention and public sentiment about an ongoing silver manipulation. For the regulators, any type of contract default in COMEX silver would be an unmitigated public relations disaster, after denying the existence of a silver manipulation for decades. This is paramount among the reasons I no longer think a COMEX silver default is in the cards.

Instead, I believe the regulators, as well as the leading players on the COMEX, would move heaven and earth to avoid any hint of a default in silver. In fact, I believe they already have done everything possible to avoid such a circumstance. As I have been reporting recently, there has been a historic short-covering by the largest commercial shorts in COMEX silver (and gold), that began the same day as the default in LME nickel, March 8.Â Far from coincidental, it now occurs to me that this unprecedented short covering by the very largest COMEX commercial shorts was intended to take a default off the table.

As Iâ??ve been reporting, the largest of the commercial shorts in COMEX silver and gold have bought back more of their short positions over the past four months than in history and as a result now hold, effectively, the lowest commercial concentrated short positions ever. Thatâ??s also the case in COMEX copper and NYMEX platinum futures. Total net commercial buying over the past four months â?? on the sharp and highly deliberate selloff orchestrated by the commercials – has been astounding.

Some 60,000 net contracts (300 million oz) in silver, 170,000 net contracts (17 million oz) in gold, 33,000 net contracts (1.6 million oz) in platinum and 67,000 net contracts (838,000 tons) in copper have been bought by commercial traders, with much-heavier than normal buying by the biggest commercial shorts. Of course, and as is always the case, the amount of commercial buying has been larger and more critical in silver, as 300 million oz represents 35% of annual world mine production â?? much greater than in the other metals referenced.

The surest way of avoiding a contract default by any exchange is to make sure there is no large concentrated short position (as Iâ??m sure the LME would now attest after its default in nickel). Thus, the historic commercial buying and reduction in the concentrated short position, not only in silver, but in other COMEX/NYMEX metals as well, has the immediate effect of greatly reducing, if not eliminating completely, the threat of a COMEX contract default. In fact, there is not the slightest doubt in my mind that eliminating the threat of a contract default was the ultimate solution for a potential problem that has existed for decades. Of course, I couldnâ??t know this back on March 8, but it sure looks clear now.

The lynch pin to my belief that the dramatic reduction in the concentrated commercial short position in COMEX silver, gold and other metals is the precursor to an epic liftoff in price is whether the big commercial shorts re-short the contracts they just bought back. Obviously, it was the commercials which orchestrated and were behind the dramatic rig job lower over the past 4 months, as they succeeded wildly in getting the managed money traders to sell and sell short in prodigious amounts. All that matters now is what the former big commercial shorts intend to do on the next rally â?? stand aside or re-short.

This is the new moment of truth, namely, will they, or wonâ??t they? Having avoided the surest path to a contract default by largely eliminating the commercial concentrated short position that has plagued COMEX silver for decades, the question has shifted to what comes next. Please understand that Iâ??m an analyst – I can slice and dice the known data to the best of my abilities, but no one can predict the future anywhere as accurately as dissecting the past. There are now very few analysts and commentators which canâ??t see the bullish set up now created by the commercials drastically reducing their short positions in COMEX silver and gold (although it still amazes me how even fewer would attribute the resultant positioning as deliberate by the commercials in hoodwinking the manage money traders).

While no one can know for sure what the big former commercial shorts will do on the next rally, once that rally occurs, I have every expectation that future COT reports will reveal what they do. My best guess is that the big former commercial concentrated shorts will not add and replace the short positions they just bought back, but I promise to accurately report whatever the former big shorts do or donâ??t do. In the interim, please allow me to restate why I think things may have changed.

The nickel default on the London Metals Exchange is, I believe, far more serious than many suspect. So serious, that I believe the LME will never be the same. Any exchange that unilaterally busts trades and suspends trading because one trader was caught out of position with too large of a concentrated short position, is not an exchange worthy of transacting business on. For sure, the LME is thedominant base metals exchange in the world and as such would not be expected to vanish overnight.But given the choice of dealing on an exchange that deliberately took sides in nickel to protect theexchange and by extension, side with the big concentrated short, is not worthy of doing business on. Infact, you would have to have your head examined to voluntarily do business on such an exchange and,as time passes, I would expect those with a choice will not do business on the LME.

You can be sure that the travails of the LME in nickel have not been lost on the CME Group (owner/operator of the COMEX and NYMEX) or on the federal regulators at the CFTC or DOJ. As Iâ??ve pointed out previously, it is now clear that the problem in LME nickel was directly related to the concentrated short position â?? had there been no large concentrated short position, there wouldnâ??t have been any problem. This is not rocket science.

I suppose my years of complaining about the concentrated short position in COMEX silver may have had some influence on the regulators (at least, the CFTC stopped saying it wasnâ??t a problem), but I am still taken aback by the timing, namely, on the day of the LME nickel default, the price tops were seen in COMEX silver, gold, platinum, palladium and copper and four months later, not only are all substantially lower in price â?? all have seen massive commercial buying and reductions in their commercial concentrated short positions. I suppose we could debate whether all this was some unusual but innocent coincidence or not, but why bother? What comes next is all that matters.

If the former big commercial concentrated shorts turn right around and add back their previous shorts on a rally in silver, then I will have been wrong in my current line of thinking. Weâ??ll still get a decent rally of as much as $5 or $10 (considering how far weâ??ve fallen), but if the former big commercial shorts turn right around and add aggressively to short positions, itâ??s hard for me to see much more of a rally. But if the former big concentrated commercial shorts stand aside and donâ??t add aggressively to short positions, then the skyâ??s the limit in silver.

Of course, I do expect the smaller silver commercials, which I refer to as the raptors and do happen to hold a very large net long position of around 40,000 contracts, to sell on a silver rally, but I am less sure about the prices the raptors might be willing to sell at. Â My best guess is that the bulk of the raptor long position has an average price of around $22 and at current prices is some $650 million underwater (their largest loss in memory). I would also imagine that some of the early silver raptor longs may have succumbed to the steep losses and have bailed out and those raptors remaining long are fairly strong hands. So, while I expect heavy raptor selling on higher silver prices, I would imagine that raptor selling wonâ??t kick in until silver prices exceed $22.

The roughly 35,000 contracts of managed money shorts added on the decline has an average cost of around $21.50 and, at current prices would indicate a collective open profit of more than $400 million, about the largest open profit by the managed money traders on the short side. Undoubtedly, on a silver price rally, the managed money shorts will not wish to turn such a large open profit into a loss and, therefore, will likely be quick to buyback and close out their open shorts. The problem for them might be a scarcity of willing sellers on a one- or two-dollar rally. The potential mismatch is between where the raptors might be willing to sell and where the managed money traders might be looking to buy.

Should the silver raptors hold out for higher prices, itâ??s hard for me to see how the managed money shorts wonâ??t be forced to reach up in price to buy back all the silver shorts they wish to buy back and close out.

In order to accommodate the expected amount of manged money short covering and new buying on higher silver prices (as many as 50,000 to 60,000 net contracts), it will take raptor long liquidation of 35,000 contracts and some other amount of selling by the former large commercial concentrated shorts. Should that selling by the former commercial concentrated shorts not be forthcoming, then a buy/sell imbalance would present itself and that could be the formula for a genuine price liftoff in silver.

The numbers in gold are similar and with a gold raptor long position of only around 12,000 contracts, might even be more critical, although the gold raptors have gone short more readily than the silver raptors in the past. Back on March 8, the gold raptors were net short 28,000 contracts. Still, it will take a lot more than 40,000 contracts of raptor net selling in gold to satisfy the expected amount of managed money buying on higher gold prices, which could easily top 100,000 contracts (considering that 150,000 contracts of managed money net selling occurred on the decline in gold prices since March 8).

Even if the former big commercial concentrated shorts add a good amount of gold shorts back, the potential for a buy/sell mismatch on a rally is high. And considering how far current silver and gold prices are below the key moving averages, that only enhances the prospects for a surge higher in price greater than typically seen. Of course, higher prices will involve managed money buying, but until those higher prices arrive, the markets are vulnerable to commercial bear-baiting to the downside.

As far as what to expect in Fridayâ??s new COT report, gold and silver prices were lower through the reporting week ended yesterday, making fresh lows and including a pretty vicious selloff last Thursday; so the â??formulaâ?• calls for further improvement (managed money selling and commercial buying) in their respective market structures. At the same time, the question of how much more the commercials can lure the managed money traders onto the short side looms large.

At this point, the upside price potential far outweighs any remaining downside potential by such a wide margin that there is little point in worrying about still-lower prices. What amazes me most is the large number of those who recognize just how bullish the market structures have gotten in COMEX silver, gold and copper, as well as in NYMEX platinum, yet are still silent or oblivious to how the bullish structures came about (through deliberate commercial price rigging). The regulators are, undoubtedly, hoping that most will remain oblivious after we make the turn higher.

At the prices prevailing as I send this, slightly lower prices in gold have reduced the total loss to the remaining big commercial shorts in COMEX gold and silver, by less than $100 million from Fridayâ??s close to $4.5 billion.

Ted Butler

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Silver – $18.65Â Â Â (200 day ma – $23.12, 50 day ma – $20.97, 100 day ma – $22.90)

Gold – $1700Â Â Â Â Â Â (200 day ma – $1843, 50 day ma – $1815, 100 day ma – $1876)

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