

## October 11, 2017 – Where's the Silver Shortage?

The other day I was asked what happened to the physical silver shortage I've been talking about for decades. Considering how much time has passed by with no shortage, it is more than a fair question. As it turns out, while a good bit of time has passed, I'm still convinced about the inevitability of a physical silver shortage and it still remains the top reason I hold silver. Let me give you the reasons for my conviction, including a special new one that's developed since I first became convinced about a coming silver shortage many years ago.

I think the first order of business is to define a physical silver shortage. I'm referring to a wholesale shortage of silver in the form of 1000 oz bars, not in coins or small bars considered to be retail. After all, there have been a series of obvious shortages in retail forms of silver over the years, including sellouts and periods of unavailability from the US Mint for Silver Eagles, the most popular silver bullion coin in the world. I'm not talking about retail silver shortages, but a coming shortage of 1000 oz bars, the industry and institutional investment standard for wholesale silver. To date, there has never been a full-blown shortage of 1000 oz bars. There was a brief time, in early 2011, when such a wholesale shortage began to develop, but the sharp break in price starting in May of that year, extinguished the budding shortage. I'll come back to this in a moment.

A good definition for shortage is a state or condition when there is not enough of an item to go around; or demand exceeding supply. Shortages are generally temporary in nature, because, sooner or later, supply and demand must come into balance. What causes supply and demand to come into eventual balance is a high enough price, which at some level will cool off demand and stimulate increased supply. This is the cornerstone of the law of supply and demand. One other thing, for commodities, a shortage is the most powerfully bullish force possible; no force could be more bullish than a physical shortage.

Applying this definition to silver, I am convinced of a coming shortage in 1000 oz bars that will last for a relatively short period of time, most likely months, but perhaps years, where the price will rise much more sharply than most can even imagine. At some point it will reach unsustainably high levels before coming back down to more realistic levels, but still much higher than current prices. Obviously, if there is going to be a wholesale shortage of silver, from an investment perspective, it will be much more rewarding for one to be positioned before that shortage becomes visible to all and reflected in price. And while I am talking about a shortage of silver in the form of 1000 oz bars, please don't misinterpret this to mean not to buy or hold silver in other forms, as all will follow the wholesale price higher.

There is nothing subtle about an actual shortage, it kicks with the price force of a mule. No such force has ever been exerted in silver, so it's not something anyone has any practical experience with. I will be the first to admit that the world has never witnessed a full-blown shortage in the wholesale form of silver and the next time one occurs will be the first time. But it would be a mistake to confuse something that hasn't occurred with something that can't occur. Even though the world has never witnessed an actual silver shortage, the prerequisites for such a shortage are and have been in place. All that's needed is a spark to set off a price conflagration.

The main prerequisite for a physical silver shortage is that it is a commodity widely consumed in

industrial and other forms of fabrication. Upwards of 90% of total annual silver production, from both mining and recycling, is so consumed. This leaves only 10% or so of annual production available for investment demand, which is the real potential driver of shortage and the price. Silver's unique dual-consumption profile, industrial and investment demand, sets it apart from all other commodities. Copper is all industrial, zero investment; gold is mostly all investment, with little industrial consumption. There's nothing quite like silver, in terms of dual-consumption.

Why this matters in terms of a coming physical shortage is because silver's investment demand can kick off an industrial user attempt to stockpile when prices start to surge due to investment buying. These industrial users simply cannot and will not tolerate any delays in silver deliveries caused by a burst of investment buying. If you think the urge for people to scramble to get stockpiles of water and food and gas before a hurricane hits is strong, then multiply by ten to gauge the force of businesses to remain going concerns by physically secure silver to keep assembly lines running. There will be no philosophical debate among the users as to what caused a delay in their vital silver deliveries, there will only be attempts to increase physical inventories, which will only exacerbate the shortage further.

The industrial user attempt to build physical inventories is what separates silver from gold. Investment demand for gold can send the price higher by leaps and bounds, but it won't trip off an industrial user inventory buying panic simply because there are so few industrial users of gold. This is not a knock on gold, just the critical distinguishing feature of the big difference between gold and silver.

The fact is that I expect future massive investment buying in both gold and silver for the simple reason that both metals seem to have been the only assets left behind in the historic monetary and debt creation of the last decade. Every other investment asset in the world is floating close to all-time highs. As to why silver and gold have performed so poorly while everything else has bubbled up has to do with the COMEX price manipulation, but that's not the topic of this piece.

But here, too, a big difference must be pointed out between gold and silver. Because silver has come to be consumed industrially for the past 100 years, world silver inventories have been decimated, while above ground gold hits new records every year. As a result of the depletion in world silver inventories and its ultra-low price relative to gold, the dollar value of all the 1000 oz silver bars in existence only comes to \$20 or \$30 billion, whereas all the gold in the world is worth more than \$7 trillion, 200 to 300 times the dollar value of silver. This means that any future investment flow into gold and silver will have a disproportionately greater impact driving silver prices higher relative to gold.

These are all reasons known to many today, so let me jump to the special new reason to expect a silver shortage which only came into being within the last six or seven years. That reason, just like everything important in the silver market today, involves JPMorgan. The single biggest reason to expect a physical silver shortage is because that's what JPMorgan expects and has positioned itself for. As much as I accuse JPM of using the silver market in an illegal manner, I've never considered the bank to be anything but shrewd and highly intelligent. JPMorgan exists for one main reason - to make as much money as it can, by any means possible.

The bank's accumulation of 650 million oz of physical silver since the spring of 2011 is the purest proof that it expects a physical silver shortage of unimaginable proportions. In acquiring so much physical silver, JPMorgan has positioned itself perfectly for the coming unprecedented shortage ahead. Everything supports this conclusion, including the public timeline.

It is now a matter of public record that JPMorgan became the dominant COMEX paper silver short upon its acquisition of Bear Stearns in March 2008 and has maintained that role to this day. At that time, silver had run up to \$21, the highest level it had been in 28 years and was inflicting ruinous margin and mark to mark losses on Bear Stearns, leading to the JPMorgan takeover. That proved to be the price high for silver for the next two years as JPM was successful in driving prices under \$9 in late 2008, making hundreds of millions and even billions of dollars on its short sales in the process.

But a budding physical silver shortage which began to exert itself in late 2010 caused prices to move higher and inflict large open and unrealized losses on JPMorgan due to its large COMEX paper short position. Silver prices raced to near \$50 by the end of April 2011, leaving JPMorgan with billions in open losses. There is no doubt in my mind that this was JPMorgan's "come to Jesus" moment, in which it came to understand the power of a physical shortage by being on the dead-wrong side of the equation. In April 2011, with silver racing to \$50 on genuine signs of a developing wholesale physical shortage, JPMorgan looked into the financial abyss and saw the light.

The light that JPMorgan saw was that a physical silver shortage was at hand and it needed to both rescue itself at that time and position itself never to be in that predicament again. It did so by arranging to help crash prices starting on May 1, 2011 to cut off the growing investment demand that was flaming the developing physical shortage (before it awakened the industrial users). Having accomplished that in spades through a variety of dirty COMEX trading tricks, JPM also set about creating not only protection against certain future silver shortages, but a way to earn enormous future profits. The only thing that could offer both permanent protection and massive profit opportunity in a physical silver shortage was to possess physical silver.

JPMorgan came to appreciate the power of holding physical silver in the way most important lessons are learned, namely, by learning it the hard way. Watching its massive paper short position nearly blow up in early 2011 was all the lesson JPMorgan needed to decide then and there to buy as much physical silver as it could for as long as it could. So perfect was JPMorgan's plan and execution that I am embarrassed to admit that I did not detect it until a couple of years after it began (but still years before anyone else). In retrospect, it was a financial plan and execution for the ages, a master move on the part of JPM, perhaps its most masterful ever.

I've been waiting for the eventual panic inventory buying by the industrial users in silver for more than three decades. Never, over that time, would I ever have imagined that a completely new and different reason would emerge to support my conclusion; but that's how I view JPMorgan's accumulation of physical silver over the past six years. When the most powerful price force possible in any commodity, a physical shortage, hits in silver causing the price to soar, JPMorgan will have the perfect opportunity to unload its massive physical stockpile with barely anyone noticing. That's what these guys do for a living and I'm hoping we can all join in for the ride.

Time to transition from what's to come, to what has occurred since Saturday's review. The new short report for stocks featured hefty reductions in the short positions on GLD, the big gold ETF and SLV, the biggest silver ETF. I can't call the large declines, particularly in GLD, surprising, having speculated a couple of weeks ago (Sep 27) that my only explanation for the then-counterintuitive large deposits of gold into GLD as prices were declining was an upcoming sharp decline in the short position. The very sharp reduction in the short position of GLD, the largest in memory, in the new report would seem to confirm my explanation.

<http://shortsqueeze.com/?symbol=gld&submit=Short+Quote%E2%84%A2>

For positions held as of Sep 29, the short position in GLD declined by nearly 6.5 million shares (650,000 oz) to 12 million shares (1.2 million oz). To be sure, there was a very large 5 million share increase in the short position of GLD in the previous report (the short reports cover two-week periods), but that just confirms those shorting shares of GLD in the previous report, then brought in and deposited metal to create new shares with which to close out the new short positions. This has been a key premise of mine in SLV for years and considering the similarity in the share structures and workings in GLD and SLV, the big deposits and the sharp increase, followed by sharp decrease in the short position of GLD fit the premise like a glove.

There was also a sharp reduction in the short position in SLV, of nearly 2.8 million shares, to just over 12.6 million shares (ounces). As a reminder, there is roughly one-tenth of an ounce of gold for every share of GLD and one ounce for every share of SLV, minus accumulated annual management fees from inception. While the short reduction in SLV was large, it didn't compare to the reduction in GLD. As to what caused the reduction in SLV, there are a variety of possible explanations, including the arbitrary close out by clerically transferring shares held short against the box. •

I would like to step back and explain why I focus so closely on changes in the short positions of SLV and GLD, even while the issue is rarely discussed elsewhere. I acknowledge that the topic can seem arcane and overly detailed to many, but the reason I persist is because these are the largest publicly-held physical stockpiles of silver and gold in the world. As such, it would be negligent not to include this data in any legitimate analysis of gold and silver.

As I've discussed previously, since shares of GLD and SLV represent a rigid proscribed amount physical metal, any short selling of shares is tantamount to shorting physical silver and gold. In sharp contrast, the long and short positions in futures contracts on the COMEX are paper derivatives in which only a very small percentage of the contracts are consummated by actual delivery. Even though COMEX contracts are predominately paper traded, so many contracts are held that this is what determines price. Where the COMEX concentrated net short position of the 8 largest traders in silver runs to 500 million oz, the total short position in SLV is currently 12 million oz. But you have to remember that the 500 million oz is paper, while the 12 million oz held short in SLV is, in essence, actual metal that's been sold short.

My real point is that I persist in trying to slice and dice the goings on in GLD and SLV from every possible angle because they must be so examined, given their structure and preeminence in the world of physical precious metals. Observing the recent large physical deposits in GLD without considering the corresponding increase and subsequent decrease in the short position would be overlooking important analytical clues which are publicly documented. Analysis is little more than observing as

many verifiable facts as possible and assembling the most important of them into the most plausible explanation for what is going on and what is likely to occur. We can't possibly see everything we wish to see in gold and silver and that's why it's imperative that we always consider what we can see - especially when the data (like the short report on stocks), is important.

On the price front, the rally that started from the new price lows hit Friday morning has continued, at least through yesterday's cutoff for the new COT report later this week. Unlike the past few reporting weeks, the price action this week was decidedly mixed; weak thorough Friday morning and strong through yesterday's close. As such, I have no firm conclusion for what Friday's COT report may indicate and will stick to examining the report and not handicapping it. (I suppose I may also be a little gun shy after last week's wide miss).

As to what has transpired over just the past few days, I would imagine managed money buying, particularly in silver where both key moving averages (the 50 and 200 day ma's) were penetrated to the upside (which wasn't especially difficult in silver, since they were the same price). Gold has yet to penetrate its 200 day moving average to the downside and came close to upwardly penetrating its 50 day moving average. Again, moving average penetration doesn't mean squat to me personally, but it sure does seem to ring the feeding bell for the technical funds.

Thus, it does seem likely that there has been managed money buying and commercial selling over the past few trading days. Whether there was net managed money buying for the reporting week will be seen on Friday. As for the possibilities for what this means going forward, I'm still inclined to believe it is most probable that the commercials are inducing the managed money technical funds to buy, so that they can be induced into selling later on lower prices. Sort of sucking the funds into buying temporarily only to flush them out on lower prices; a temporary counter-position trade. This does involve the 8 big commercial shorts tolerating an increase in their combined unrealized loss in gold and silver. At yesterday's close, the two day increase in the big 8's combined open loss was \$500 million, bring the total open loss to \$600 million from Friday's close. That's still way down from the \$2.7 billion the big 8 were out a month ago, so it wouldn't appear that the big 8 are in any financial difficulty yet.

It's also possible that the counter-trend rally may continue if the commercials are desirous of adding still more gold and silver short positions and are willing to tolerate increased open losses temporarily. Finally, it's always possible that it turns out completely different in that the commercials get overpowered to the upside, amid a commercial double cross by JPMorgan thanks to its massive physical position in silver. Since JPM's paper short position in silver is still quite high, I'm not leaning to JPM letting her rip at this point; but these guys are so diabolical that you never know for sure what they might be up to. In any event, this last possibility, should it occur, will have occurred for the very first time.

Ted Butler

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Silver – \$17.17 (200 day ma – \$17.13, 50 day ma – \$17.13)

Gold – \$1292 (200 day ma – \$1252, 50 day ma – \$1300)

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