September 20, 2023 – The Bonfire of the Silver Shorts

After 40 years of silver price manipulation and suppression on the COMEX, the physical market has experienced a lack of production growth and enhanced demand brought about by too-low silver prices. According to the immutable law of supply and demand, silver is now in a deepening physical shortage in which sharply higher prices are both required and inevitable. The key element that I speak of today is the likely behavior of the short sellers of silver derivatives. Investors hold 2 billion ounces of silver in industry-standard 1,000-ounce bars and a similar quantity in smaller bars and coins. Since these holdings are owned outright, there is no short position as exists in every derivatives contract, including COMEX futures and options and OTC swap contracts.

The derivatives short positions are mostly on the COMEX, in the form of short sales in futures, call options contracts and also in OTC dealings. Thanks to detailed information provided in the weekly Commitment of Traders (COT) reports, great clarity is given to the potential exposure of the short sellers in COMEX silver futures contracts. The current total open interest in COMEX silver futures (minus spreads) is around 110,000 contracts, or 550 million ounces.

Again, thanks to the detailed data provided in the COT reports, we further know that the 8 largest commercial shorts hold more than 50,000 contracts net short or the equivalent of 250 million ounces. Other traders in the commercial, non-commercial, and non-reporting categories hold 300 million ounces short. This current net short position of the 8 largest shorts, at 250 million ounces is of extreme danger to them should silver prices explode, as I believe is in the cards.Â Often overlooked is the even larger 300 million oz short position held by those outside the big 8â??s holdings.

Then, there are the long and short positions held in COMEX silver call options, most of which are â??out-of-the-money,â?• meaning they wouldnâ??t result in great danger to the short sellers of these options until and unless silver prices rose sharply. Conservatively, the true exposure of the call options on the COMEX is â??onlyâ?• 25,000 contracts of the more than 70,000 contracts of total call option open interest. That would bring the total COMEX futures and call options short exposure to 135,000 contracts (110,000 futures contracts plus 25,000 call options contracts) or 675 million ounces.

That means, for every dollar increase in the price of silver, the longs would make $675 million and those short would lose $675 million. A $5 price increase would amount to a $3.4 billion gain and loss, while a $10 increase would amount to a collective gain and loss of $6.75 billion. Should the price of silver increase much more than that, as I believe, the math is astounding for collective gains and losses. The short-sellers of silver would face a cataclysmic financial setback. For the longs, it would be the stuff of dreams â?? with unimaginable money and profits raining down from the heavens.

However, for those short, it would be a terrifying financial nightmare. The 675 million ounces held short on the COMEX is mostly held on a margin basis, and should silver prices explode higher, as is inevitable and likely imminent, a margin call â??hellâ?• scenario would develop.Â Virtually all silver shorts will be subjected to daily and perhaps intraday demands to deposit untold additional amounts of margin money with little time to do so. In a sharp price rise of the type I envision, the brokers holding the short positions will not hesitate to buy back customers short positions with little prior notice adding additional upward pressure to silver prices.

In addition to the net short derivatives position on the COMEX in silver futures and call options, there is the matter of those short call options on SLV, the big silver ETF, where the true net exposure could easily top 200 million ounces. Finally, there is the OTC derivatives market, where I allege that Bank of America, alone, may have a short exposure of a billion ounces of silver. Thatâ??s more than the combined short exposure on the COMEX and in SLV. Iâ??ve complained to the S.E.C. and the Office of the Comptroller of the Currency about BofAâ??s egregious short position in silver OTC derivatives. In fact, the response I received from the OCC did not dispute my contentions and seemed to confirm them.

https://silverseek.com/article/occs-response

As a commodities broker for many years, I have lived through and observed the type of cataclysmic market events and the effects on those on the wrong side of highly leveraged derivatives positions. A comparable event that comes to mind was the sudden sharp selloff in the stock market in October 1987, when the Dow Jones Average fell nearly 25% in a day. I personally knew many who had large short positions on put options on stocks, that to that point had been extremely profitable, until the stock market broke sharply and the losses suddenly became insurmountable to the point of bankruptcy. Â A more recent example was the meme stock episode of early 2021, when a stock like GameStop rose by more than 25 times in a few months due largely to short covering.

One of the unintended consequences of the 40-year COMEX silver manipulation and the failure of the regulators (both the CFTC and the industry self-regulator, the CME Group, Inc.) to end the manipulation earlier, is that it has lulled those short into believing the current price is somehow normal (otherwise no one would be short). However, just as there is no force more powerful on the price of a commodity than a physical shortage, there is no force more powerful in the world of derivatives than a short-covering panic. The impact on price brought about by an inevitable short covering buying panic in silver promises to be epic.

Turning to other matters, there was a rather large deposit of nearly 9 million oz on Monday into the big silver ETF, SLV, largely reversing the recent redemptions/withdrawals over the past two months. In fact, the silver holdings in SLV are now back to where they were at the beginning of August (450 million oz), after dropping by 15 million oz until the past 2 weeks. Mindful that I may be guilty of confirmation bias (seeing what I want to see), I have been contending since the beginning of the year that there is a limit as to how far the combined holdings in SLV and in the COMEX warehouses could fall, since the vast bulk of the metal was held by investors. However, the combined holdings did fall, first to around the 730 million oz level and more recently to as low as 714 million oz (last week). Now back to 724 million oz, as a result of this weekâ??s big deposit, it will be interesting to continue to plot the combined holdings.

As far as what was behind this weekâ??s large deposit, the most plausible explanation would appear to be it was intended to reduce the rather large short position on SLV (close to 29 million shares). Even if the large deposit was intended to reduce the short position, it would not involve the next short report next Tuesday (Sep 26), due to reporting period cutoffs, although there were some notable deposits made over the reporting period to be featured in next weekâ??s report. However, the short report on SLV is notoriously difficult to predict (at least for me).

If you recall, back in January, there was a very large deposit of metal into SLV (20 million oz), which looked intended to reduce the large short position at the time (45 million shares+). Instead, it took until April for the short position to fall by an equivalent large amount, which I explained at the time was likely due to a â??short against the boxâ?• transaction which allows a short position to remain open, even though it was effectively covered in January, but not closed out until April. The sequence was described in detail at the time and is available in the archives.

Of course, all eyes are focused on recent price action in silver and gold in regards to likely positioning between the commercials and the managed money traders as the latest moving average drama plays out, enhanced by todayâ??s latest Federal Reserve actions. As always, I find any announcements by the Fed, along with the typical things attributed to silver prices as in the nonsense category, but admit they do provide convenient cover stories for whatever the resultant price action may be.

However, I am particularly mindful of the current potential for a silver price explosion, given the extremely bullish positioning set up on the COMEX. The latest recent deliberate plunge below all the key moving averages has all the appearances as creating upside moonshot potentials for silver and gold. In other words, the collusive COMEX commercials look like they positioned the managed money traders for big doings on the upside. Accordingly. I think Fridayâ??s new COT report will feature additional improvement or at least no serious deterioration, despite silver prices being mostly unchanged over the reporting week. Gold prices did rise by as much as $25 over the reporting week, so I am less sure there, although any deterioration (managed money buying and commercial selling) should be modest, if we get any at all.

In silver (and very much in the hoped-for department), I think we could see some big 4 short covering into raptor long liquidation, an admitted long-time fantasy of mine and at the top of the list of my personal confirmation biases Â – the one that holds the 4 big shorts would turn buyers to the upside as the big move higher unfolds. Now, whether I get to witness this personal fantasy or not, the absolute key element here is to whether these big 4 shorts add aggressively to short positions should we move higher from here. I wonâ??t beat around the bush, if they do add aggressive to shorts that does put the rally in question. If they donâ??t, we explode in price.

Likewise for the fate of the silver shorts, where the greatest liability and danger rests, unfortunately, on the backs of those shorts apart from the big 8 COMEX shorts. If the 8 big shorts lean into the developing rally by aggressively adding shorts to cap and contain the budding silver rally, then the hundreds of millions of ounces of silver derivatives contracts held short by the unsuspecting non-big 8 shorts, may be temporarily spared the financial disaster that awaits them. If the big 8 donâ??t add aggressively to short positions, the financial nightmare for the unsuspecting shorts goes real-time.

It comes down to whether one thinks the current price of silver represents the true free market price according to the actual law of supply and demand and not some artificial price weâ??ve gotten used to following decades of artificial COMEX price-setting. Obviously, those short silver donâ??t suspect, in the least, that the price has been artificially manipulated â?? otherwise they would never be short. But if the price wasnâ??t artificially suppressed and manipulated, then why are we seeing signs of physical shortage abound and clear evidence that the short positions in silver derivatives seem excessive and dangerous to the shorts in numerous data points?

Furthermore, since there is no way on Planet Earth can those collectively short way more than a billion ounces of silver derivatives hope to ever acquire the physical silver necessary to close out their short positions by actual delivery, that leaves only the buyback on the various markets of the open short positions as a solution for closing out the massive amounts of shorts. Â While we await the answers to these questions, it would seem quite dangerous and ill-advised to be short in the interim.

The question on most minds this day is how the markets, particularly silver and gold, would fare on this Fed decision-day. Certainly, the price action and trading volume up until the announcement and press conference couldnâ??t have been better according to everything I look at, namely, prices drifting up into the critical moving averages in both gold and silver and not on excessively large trading volume â?? meaning not much positioning change. This was the best outcome possible in my mind. What would the actual announcement and press conference bring?

Well, there was a fairly shallow price dip in silver and gold on the announcement and into the start of the press conference, but much less than as seen in the past and trading volumes remained light overall in silver, both in terms of on the COMEX and in SLV and other silver ETFs, while gold volumes are slightly elevated in ETF trading, as well as on the COMEX. Prices have rebounded from the initial shallow selloffs, although not to the point of establishing new daily and recent price highs. All in all, gold and silver price action has been quite favorable for Fed decision days and we still are set up quite favorably for significant new price highs ahead.

Ted Butler

September 20, 2023

Silver – $23.70Â Â Â (200-day ma – $23.58, 50-day ma – $23.90, 100-day ma – $23.93)

Gold – $1962Â Â Â Â Â Â (200-day ma – $1931, 50-day ma – $1955, 100-day ma – $1964)

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