
The Commitments of Traders Bible

*How to Profit from
Insider Market Intelligence*

STEPHEN BRIESE



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The Commitments of Traders Bible

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*To my father,
E. Elliott Briese
(1924–1991)*

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Preface

The Commodity Futures Trading Commission's weekly *Commitments of Traders* (COT) report is the single most revealing internal market report issued by any government agency. It single-handedly establishes U.S. futures as the most transparent of any of the world exchanges. In the process, it promotes a level playing field for commodity and futures traders, large and small.

The COT's application extends well beyond the confines of the commodity pits and into virtually every market sector, from FOREX to gold stocks, from equities to treasuries, and from ETFs to sector funds. The world is interconnected, and it runs on commodities, currencies, and financial paper—all traded on the U.S. futures markets.

Think I exaggerate? In 2006 the Commodity Futures Trading Commission (CFTC) asked for public comments regarding extending or eliminating the COT report. They received a record 4,659 responses from 22 countries, every one encouraging the CFTC to continue and expand their report—with one notable exception. In a letter to the Commission dated August 26, 2006, the International Swap and Derivatives Association objected on behalf of its "725 member institutions," noting that "Market participants, including speculators, with such information on non-traditional commercial trends, would gain a competitive advantage allowing them to trade ahead of the swap dealers." If the largest derivative traders in the world are afraid of your having access to this intelligence, you had better take notice.

Despite their objections, the new *COT-Supplemental* report on swap dealers began weekly publication on January 8, 2007. The bad news is that this added 506 new data points to the more than 17,000 individual data points already contained in the weekly COT reports. The good news is that there now is a guide.

This book is your manual. Without it, you are at the mercy of the junior wire services reporters who get stuck working Friday evening, or of the ramblings of would-be COT mavens posted on bulletin boards around the Internet. Armed with this book, you have a chance at separating the wheat from the chaff. Without it, you will get the chaff. That, in a kernel, is the case for this book.

WHAT IS THE *COMMITMENTS* REPORT?

You can think of the COT as a sentiment indicator, but instead of opinion surveys, it is based on the actual market positions of the largest futures traders. You can also think

of it as a fundamental indicator, because it lets you know the market positions—and therefore the price outlook—of the firms who operate in the cash markets and who use futures to hedge price risk. When these market insiders move to one side of the market en masse, even swap dealers and hedge funds can get flattened.

If you are among the largest traders in the crude oil or dollar pits in New York, or the S&P or Bond pits in Chicago, you report your position to the CFTC on a daily basis. The CFTC totals these up each Tuesday, separating them between hedger and speculator, and publishes the totals on Friday afternoon. Watching the COT report, you can see when the trade forms a consensus that prices have moved too far away from fundamental values, or find out when the hedge funds have all piled into one side of the market and are about to have their hat handed to them. This is insider information, legal insider information, and if you are trading without it you are starting out every week already behind.

Analyzing the *Commitments* report has been my little niche for more than 20 years. I have subscribed to the *Commitments* report since 1974, and since 1988, have been writing exclusively about the COT—for paid subscribers to my *Bullish Review of Commodity Futures Markets* market letter. Some have subscribed since the first issue, unusual longevity in futures trading. In the early 1990s, I wrote several magazine articles (for *Barron's*, *Stocks and Commodities*, and *Futures* magazine), which helped bring public attention to the *Commitments* report. And in 1998 and 2002, I gave a series of private seminars in the United States and Canada, which were the starting point for this book.

The COT report provides essential insider market intelligence that cannot be found in any other source. Its applicability goes far beyond the U.S. futures markets it covers. This book lists hundreds of securities from all over the world whose prices are highly correlated with commodities contained in the COT report. It should not be surprising, given the interconnecting world markets and heavy dependence on commodity production and trade. You probably would assume that Precision Drilling or Apache Corporation's stocks are 96 percent correlated to the price of oil. If you can predict price trend changes in crude oil using the COT data—and I think I can convince you of that—these signals are also applicable to Apache's stock or *hundreds* of other issues that trade in lockstep with the price of oil. The popularity of commodity index funds, and commodity- and currency-based sector and exchange traded funds multiplies the audience for the COT report.

WHO USES THE COT DATA?

I wanted to include a chapter on how real traders and investors incorporate the *Commitments* data into their market approach, so I put out a request to my subscribers to share their insights. These people are not a bunch of strangers; some of them have been with me for 20 years, and I have met hundreds of them at my seminars. I received just two responses, both brand-new subscribers. For some reason, those who know best the value of these reports do not want to share. I can tell you that my subscribers range from small speculators to commercial hedgers, and from individual traders to some of

the largest hedge fund and institutional investment managers in the world. I just cannot tell you (firsthand) *how* they use it—with one exception.

A commodity fund manager I have become well acquainted with has been quite successful using the COT Index to screen futures market positions. His belief is that a consensus among large commercial hedgers can be used to spot major trend changes ahead of traditional sentiment or technical indicators. He looks for a commercial buying extreme (100 percent COT Index) as a setup for long positions, and a commercial selling extreme (0 percent COT Index) to signal a short setup. Once the COT Index reaches an extreme, he uses a technical trigger (together with an overriding risk filter) to enter a trade in anticipation of the new trend. Although the technical trigger has evolved over time, the COT setup has been the same for 15 years. (*Note:* This is not a generic COT Index calculated using an arbitrary look-back period. The fund manager uses the COT Indexes available at www.CommitmentsOfTraders.ORG.)

HOW THIS BOOK IS ORGANIZED

Part I, *COT Theory*, takes you through a brief history of the *Commitments* report, which has been around in its current form for 45 years, to understand how its interpretation has evolved over time. Next you will meet the players behind the numbers and see how they are broken down in the report. Then I will try to disabuse you of some common misconceptions and dead-end ideas that keep circulating around the COT report.

Chapter 5 is the most important in the book. You will find that the simple net position graph distills the dozens of numbers published on each market to expose how the biggest and smartest market insiders are positioning themselves. They can run, but they can't hide.

There are two chapters dealing with understanding the one simple indicator, the COT Index, that is the mainstay of *Commitments* analysis. If you learn how to properly view this indicator, which I disclosed publicly in 1990, you can avoid the traps that most casual (and a lot of not-so-casual) observers fall into.

Who makes the money in the futures pits? Chapter 8 is an overview and summary of 50 years of economic studies that offer compelling evidence of who wins, who loses, and why—and how to use this knowledge to ride the coattails of winners. In Chapter 9 we come down from the ivory towers and get real in the pits trying to capitalize on what we have learned.

The next two chapters are for technicians and chartists, exploring some methods of incorporating COT analysis with existing methods.

Part II, *COT in Practice*, is a detailed sector-by-sector, market-by-market reference that discusses the individual market idiosyncrasies and patterns that I have encountered time and again over the past 30 years. I also present tables full of securities that are highly correlated to each futures market. These equity, currency, and debt markets are not my specialty, but they may be yours. If so, this will give you a starting point for using the COT data over a wide range of markets. Long-term charts of trader positions are provided for

35 key futures markets. The final chapter includes the specific charts and intelligence that the swap dealers don't want you to have.

Two appendixes are provided. Technicians who wish to explore alternative ways of presenting the net position charts will be interested in Appendix A. You should be wary of any COT data source (especially the CFTC's website) until you read Appendix B.

You will find a comprehensive glossary in the back of the book, along with a list of reference material that has taken more than 30 years to accumulate. Those interested in further research will find plenty of resources.

GETTING STARTED

The book is organized as I would organize a seminar. You should not get lost if you start at the beginning and proceed chapter by chapter. There may be more information than you think you want to know. My goal is not just to give you a couple of war stories and a doorstep, but to convince you that regardless of your trading or investing methods, and no matter what markets you are interested in, there is a *Commitments* report that you should be reviewing every week, religiously. There are no proprietary secrets or come-ons—it is all here in explicit detail. More important, the book is designed to impart *how* to think about the COT data, which is more valuable than all of the “secret” formulas and trading systems you will find on the Internet and in trader magazines. Those who invest the time and effort to grasp this material cannot help but gain a trading edge unavailable anywhere else.

STEPHEN BRIESE

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S.B.

The Commitments of Traders Bible
