My Position

BY STEVE BRIESE AND LARRY WILLIAMS

Wake up! The COT report is under attack!

The Commodity Futures Trading Commission (CFTC) publishes a weekly tell-all report that discloses the aggregate futures and options holdings of large traders. It now is asking for public comment on a series of proposals that includes halting publication of the Commitments of Traders (COT) reports. Think it's not serious? Here's a part of the formal request:

"The Commission is seeking comment as to whether it should stop publishing the COT reports altogether if it is determined that either: (1) There are data anomalies in the reports for which no satisfactory solution can be found; or (2) the data in the reports provide no public benefit.

"The COT reporting program is not mandated by either the Act or Commission regulations. Therefore, if, after reviewing the comments received in response to this notice, the Commission decides to take any action with respect to the COT reporting program, it can do so without further notice or opportunity for comment."

For more than 30 years, commodity traders and investors have had a distinct advantage over their stock counterparts; we knew what the big guys were doing, thanks to the COT report. Years ago the report was issued monthly with an 11- to 12-day delay. Now we get it every week with only an inconsequential three-day lag. Larry's been using this data since 1968 and has found nothing more helpful in understanding future market direction. That's correct, nothing.

This report has enabled the average trader to spot some great market moves like the 2006 bull market in gold and the recent slide in stock prices. Year after year, this report has provided the public with full disclosure of what large and powerful traders and interests are doing in the market place.

It does not matter if you trade soybeans or the Swiss franc, the information allows all players in the pits to understand the balance of power and help them align themselves with the largest players in the game. Countless bull and bear markets have been heralded by this information. To stifle it would be to conceal insider activity.

In lectures throughout the world, people are amazed and

Using the COT Report

1. The COT report alerts traders to sudden position changes that would indicate a reversal in sentiment by a particular trader group. Also, it provides a look at total positions against their historical ranges to identify sentiment extremes among the various trader groups.

2. The size of the commercial long and short totals, and the ratio of these, is useful in discovering extremes or significant changes in sentiment within the "trade." Historically, large one-sided positions among commercial traders has indicated a potential price trend change in the direction of the commercial position. Likewise, resumptions in major trends often follow a large change in commercial buying or selling patterns.

3. Non commercial large traders have historically shown a preference for momentum trading strategies, and thus, provided the buying power in bull trends and the selling power in bear trends. It's helpful to look for a trend to accelerate in the direction of predominant one-sided large speculator trading. When net positions approach historical long or short extremes, anticipate a potential trend reversal as large speculators are nearing their risk capital limits.

4. In uptrends, the extent that large non commercial traders are willing to bid forward futures prices to a premium versus normal carrying charges gives a trader an indication of the potential strength and longevity of bullish conditions. In downtrends, momentum selling usually results in large speculators holding shorts and net short positions near their historical extremes at price bottoms in both futures and cash prices.

(The Haig working paper on the CFTC Web site lists 41 related scholarly works, many apparently using COT data, and this is probably not acomprehensive list.)

Because the large traders are not identified, only the *CFTC can judge the need for additional trader categories.* It is difficult to understand the distinction the CFTC draws between non commercials and non traditional commercials. Under the CFTC's rules a hedge fund buying futures contracts is listed as a speculator and is subject to position limits. However, if the same hedge fund acts through an intermediary swap dealer, it can apparently operate without limits and the futures position is categorized as a Commercial under the guise that the swap dealer is now a "bona fide hedger." If the CFTC does not view these as equivalent speculative (non commercial) positions, then it should be listed under a separate category and reserve the commercial category for traditional hedgers.

NOTE: For a fuller discussion and complete copy of the letter to the CFTC, go to: www.InsiderCapital.com or www.ireallytrade.com/homepage1.htm.

astounded to know there is this much transparency in the United States futures markets. They wish they had this report! And the CFTC should be encouraging such transparency by its overseas counterparts, not closing its books to the public.

Futures markets have finally escaped their notorious reputation and are considered a legitimate asset class and investment vehicle. It would be a huge step backward to no longer make this valuable information available, and would suggest to the public that insiders are at work here, who do not want their market positions known.

The thrust of the CFTC's request notice (see "Taking all Comments," below) is that for the past 15 years, the CFTC has granted certain exemptions to the speculative trading limits imposed on commodity pools, commodity funds, hedge funds and individual traders. The CFTC refers to those so-exempted as "non traditional hedgers." Once qualified as hedgers, they are automatically classified as "commercial traders" in the COT report. The number and size of these exemptions has mushroomed since 2002, in the form of ETFs, ETNs, commodity index funds and swap dealers. As many commodities moved to multi decade highs, the CFTC concedes that "questions have been raised" about their classification protocol. This request for comment is designed, in part, it appears, to blunt the impact of charges that unrestrained futures investments by "non traditional hedgers" is a major factor in the commodity run up.

Even through the CFTC acknowledges 460,000 viewings of the COT report at its Web site last year, it makes clear that it has the power to cease publication without notice. It also has the ability to effectively gut the report as it did in 1982 when the CFTC last made changes. In that instance, it suspended publication for 18 months to retool the report. It was five years before we could accumulate enough historical data to intelligently analyze the COT report again! If you favor level playing fields in the futures pits and don't want to lose this valuable market insight, you need to tell the CFTC now. Comments are due to the CFTC by August 21. There won't be a second chance to save the COT report.

Steve Briese and Larry Williams have been students of the Commitments of Traders report for more than 30 years and are *perhaps its best-known analysts.*

Taking all comments

These are the main questions posed by the CFTC. Interested parties are also welcome to address other topics or issues they believe are relevant to the COT reports.

1. What types of traders in the futures and option markets use the COT reports in their current form, and how are they using the COT data?

MORE SPECIFICALLY:

(a) How do traders use the COT information on commercial positions?

(b) How do they use the COT information on non commercial positions?

(c) In particular, with respect to information on non commercial positions, what information or insights do traders gain from the COT reports regarding the possible impact of futures trading on the underlying cash market?

2. Are other individuals or entities (academic researchers or others) using the COT reports, and if so, how?

3. Do the COT reports, in their current form, provide any particular segment of traders with an unfair advantage?

4. Should the CFTC continue to publish the COT reports?

5. If the CFTC continues to publish the COT reports, should the reports be revised to include additional categories of data — for example, non traditional commercial positions, such as those held by swap dealers?

6. As a general matter, would creating a separate category in the COT report for "non traditional commercials" potentially put swap dealers or other non traditional commercials at a competitive disadvantage (because other market participants would generally know that their positions are usually long, are concentrated in a single futures month and are typically rolled to a deferred month on a specific schedule before the spot month)?

NOTE: The full request for comment can be seen at http://www.cftc.gov/foia/fedreg06/foi060621a.htm.