



## Commitment of Traders – How to Follow the Professionals

It's not the Holy Grail – but the Commitment of Traders report gives an insight into valuations and what levels the Professionals consider over-bought and over-sold.

*"Your COT Oscillator is so simple, it's ingenious!" Michael M.*

Summary of what you'll learn in the feature article below:

- The Commitment of Traders Report tells you what the Professionals are doing. In the Report they are classified as 'Commercials'.
- The Commercials spend most of their time hedging the market, however, when strong trends develop they switch to trend following.
- TradeStation now has Commitment of Traders data built-in to their data feed. Indicators can now be easily written to analyze the Commitment of Traders data.
- If you trade Eminis don't follow the Emini (ES) Commercials. Instead follow the "full-size" contract (SP) Commercials – they are a more reliable indicator.
- Over-bought and over-sold levels can be identified by comparing changes in price with changes in the Commercials' net position. Follow the S&P directly as well as related markets such as Crude Oil, Bonds and the US Dollar.
- The Professionals have been short the market before every stock market crash from 1987 onwards. A simple Crash Warning indicator is included in the free code.
- If you don't have time to analyze the Commitment of Traders Report every week then [subscribe](#) to this site's free newsletter.

## What is the Commitment of Traders Report?

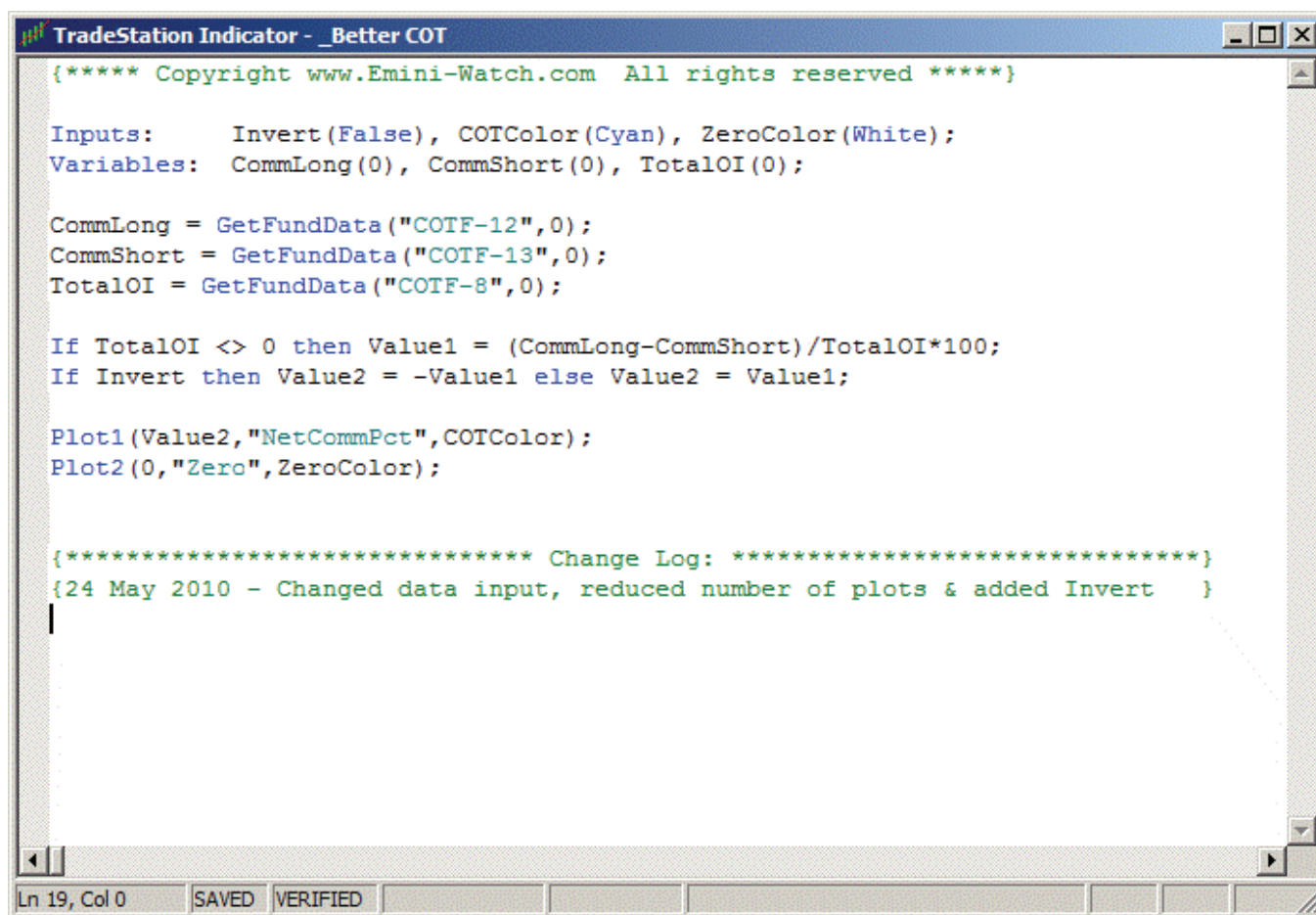
	A	B	C	D	E	F	G	H	I	J
1	Market	As_of_Date	Report_Date	CFTC_Contract	CFTC_Member	CFTC_Report	CFTC_Contract	Open_Interest	NonCommercial	NonCommercial
2	WHEAT -	080527	27/05/2008	001602	CBT	00	001	358385	83146	8410
3	WHEAT -	080520	20/05/2008	001602	CBT	00	001	369030	91522	8529
4	WHEAT -	080513	13/05/2008	001602	CBT	00	001	362266	88463	8238
5	WHEAT -	080506	6/05/2008	001602	CBT	00	001	366596	91441	7839
6	WHEAT -	080429	29/04/2008	001602	CBT	00	001	365119	88013	6849
7	WHEAT -	080422	22/04/2008	001602	CBT	00	001	369369	93207	6738
8	WHEAT -	080415	15/04/2008	001602	CBT	00	001	379563	92002	6699
9	WHEAT -	080408	8/04/2008	001602	CBT	00	001	378560	89544	6177
10	WHEAT -	080401	1/04/2008	001602	CBT	00	001	380186	93078	6200
11	WHEAT -	080325	25/03/2008	001602	CBT	00	001	393930	91859	6086
12	WHEAT -	080318	18/03/2008	001602	CBT	00	001	406703	93139	6448
13	WHEAT -	080311	11/03/2008	001602	CBT	00	001	408559	92551	6475
14	WHEAT -	080304	4/03/2008	001602	CBT	00	001	397308	95174	6940
15	WHEAT -	080226	26/02/2008	001602	CBT	00	001	426889	102564	7204
16	WHEAT -	080219	19/02/2008	001602	CBT	00	001	437456	103601	8349
17	WHEAT -	080212	12/02/2008	001602	CBT	00	001	449237	104265	8454
18	WHEAT -	080205	5/02/2008	001602	CBT	00	001	462934	100606	7590
19	WHEAT -	080129	29/01/2008	001602	CBT	00	001	454860	97831	7873
20	WHEAT -	080122	22/01/2008	001602	CBT	00	001	451429	101943	7778
21	WHEAT -	080115	15/01/2008	001602	CBT	00	001	448274	110631	8188

*Commitment of Traders: Raw Data from CFTC*

The Commitment of Traders (COT) Report breaks down Open Interest for all traded futures contracts into Long and Short positions by type of player. The people to follow most closely are the large, professional traders or 'Commercials'. They are considered the "smart money" and can give you valuable clues as to future market direction.

The Commitment of Traders data is collected weekly after the close on Tuesday and the Commitment of Traders Report is published after the close on Friday. You can find the weekly Reports on the CFTC (Commodity Futures Trading Commission) website in text and spreadsheet formats. I use the 'Compressed – Futures Only Report' in [Excel format](#). Once you've downloaded and unzipped the Excel spreadsheet, the raw Commitment of Traders data looks like the screenshot above.

## Commitment of Traders Data is Now Available in TradeStation



```
{***** Copyright www.Emini-Watch.com All rights reserved *****}

Inputs:      Invert(False), COTColor(Cyan), ZeroColor(White);
Variables:   CommLong(0), CommShort(0), TotalOI(0);

CommLong = GetFundData("COTF-12",0);
CommShort = GetFundData("COTF-13",0);
TotalOI = GetFundData("COTF-8",0);

If TotalOI <> 0 then Value1 = (CommLong-CommShort)/TotalOI*100;
If Invert then Value2 = -Value1 else Value2 = Value1;

Plot1(Value2,"NetCommPct",COTColor);
Plot2(0,"Zero",ZeroColor);

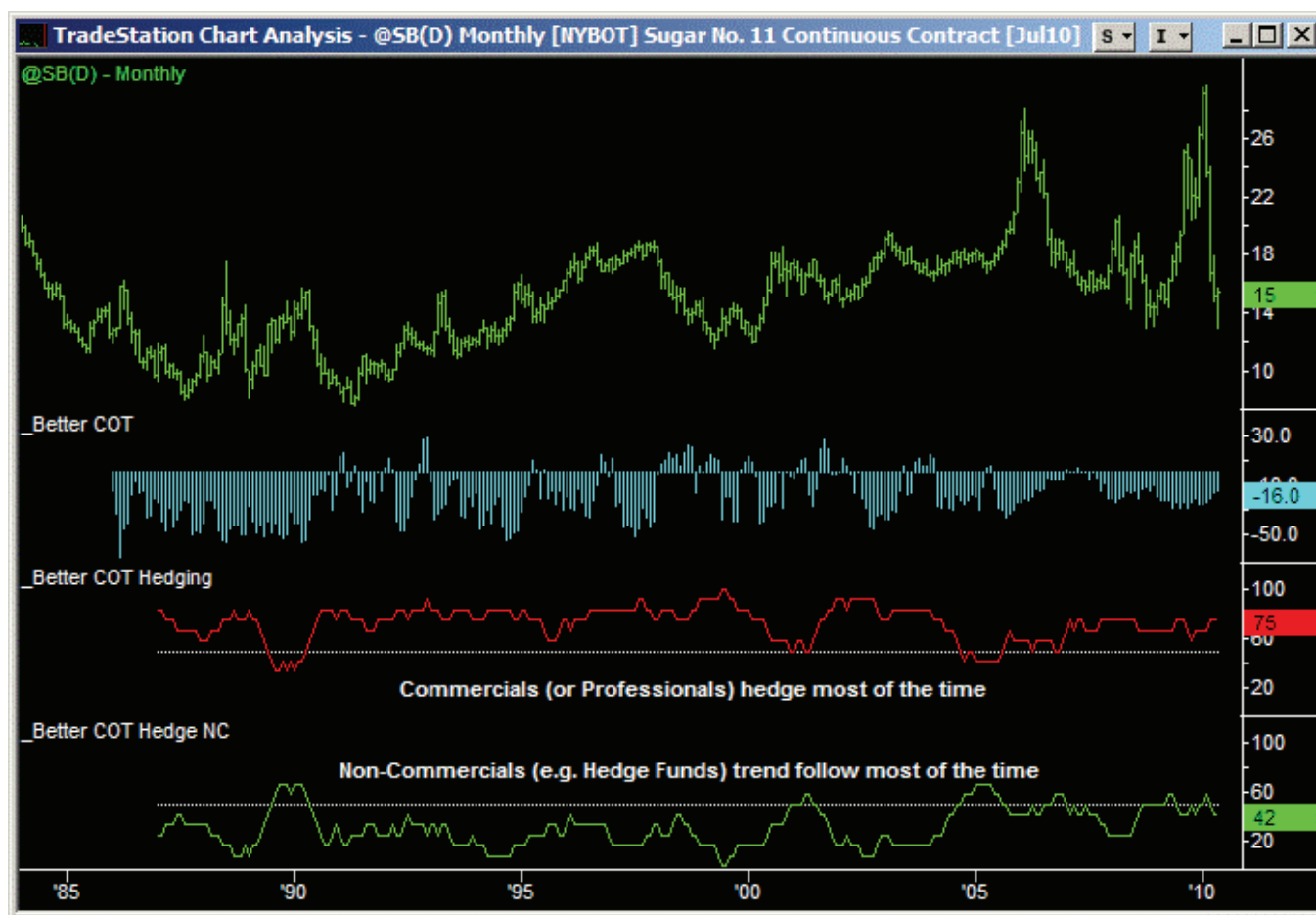
{***** Change Log: *****}
{24 May 2010 - Changed data input, reduced number of plots & added Invert }
```

### *Commitment of Traders: Calling Data in TradeStation*

Commitment of Traders data is now available within TradeStation. The code to access the data is quite simple and uses the "GetFundData" function. The code sample above calls the Commercials Long, Commercials Short and Total Open Interest data. Then calculates the Commercials net position as a percentage of total Open Interest.

This is a huge improvement on the old-fashioned method of accessing Commitment of Traders data with TradeStation. It required importing the data via an Excel spreadsheet and then using a look-up data function in indicators.

## The Commercials (or Professionals) Hedge Most of the Time



*Commitment of Traders: Hedging and Trend Following*

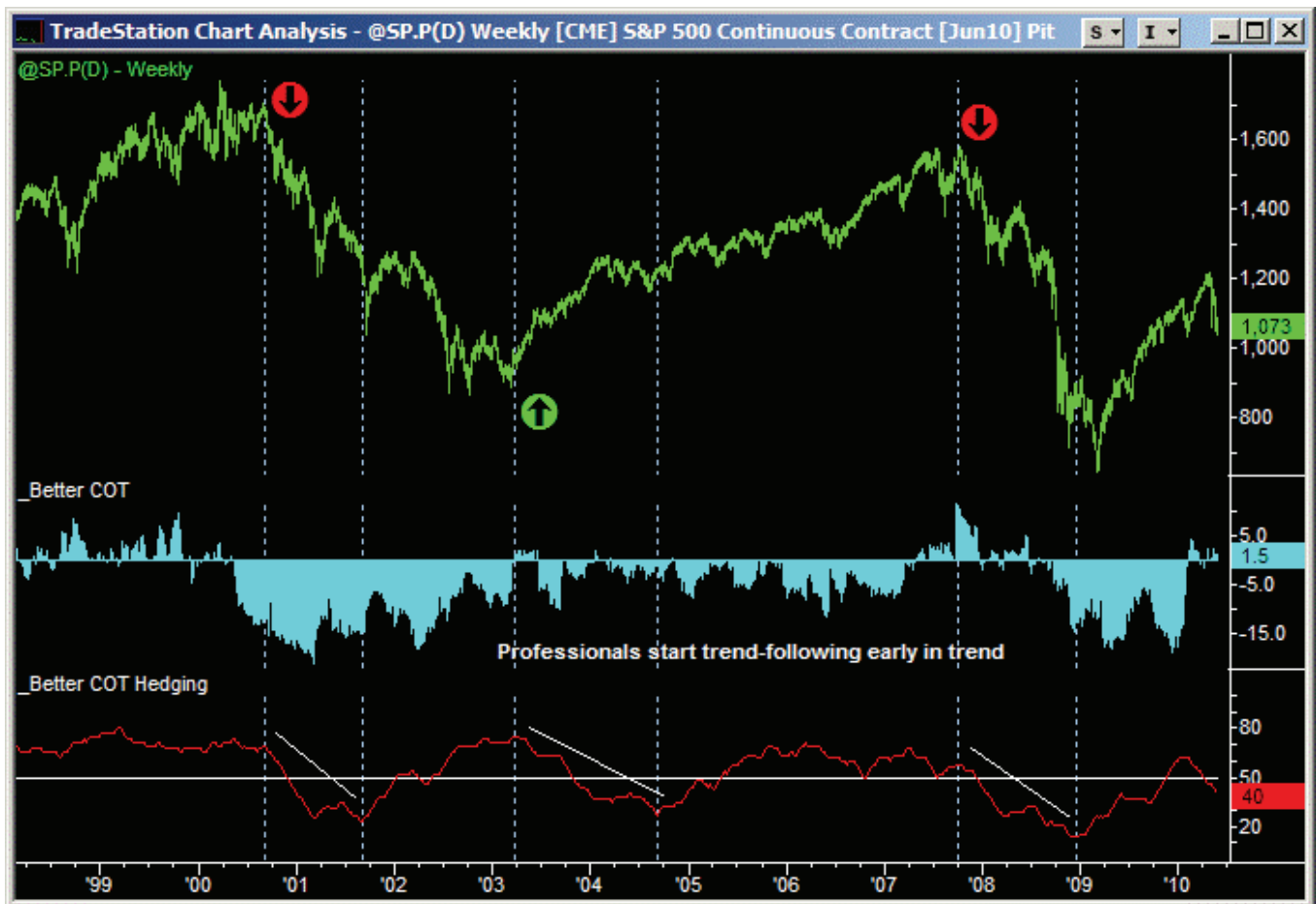
The monthly chart of Sugar above shows the Commercials (or Professionals) net position from 1987 to 2010, labeled Better COT. It fluctuates from Short (negative) to Long (positive) but has an overwhelming Short bias.

Below Better COT is a second indicator that calculates the percentage of the time that the Professionals are "hedging". I define hedging as going Short when the market rises and vice versa. For example:

- A farmer sees the price of his agricultural commodity rise. By going Short he "locks in" that price and hedges his exposure to falling prices.
- A manufacturer sees the price of his raw material fall. By going Long he "locks in" that price and hedges his exposure to rising prices.
- An importer sees his currency strengthening. By going Short he "locks in" that forex rate and hedges his exposure to a weakening currency.
- An exporter sees his currency falling (making him competitive). By going Long he "locks in" that forex rate and hedges his exposure to a strengthening currency.

In the chart above you can see that the Commercials spend most of their time hedging. The non-Commercials (typically large Hedge Funds) do the reverse and spend most of their time trend following. This pattern can be seen in all commodity and forex markets (see the video above).

## In Strong Trends Commercials Start Trend Following



*Commitment of Traders: Trend Following in S&P Futures*

The other pattern that you see in the Commitment of Traders data is that when strong trends develop the Commercials flip from hedging to trend following.

This pattern is particularly pronounced in the S&P futures. The chart above shows that since 2000 the Professionals have started trend following three times:

- In 2000 at the start of the "Tech Wreck" market decline
- In 2003 at the start of the market recovery driven by low interest rates, and
- In 2007 at the start of the "Sub Prime" market crash

Then as the trend loses steam the Professionals switch back into hedging.

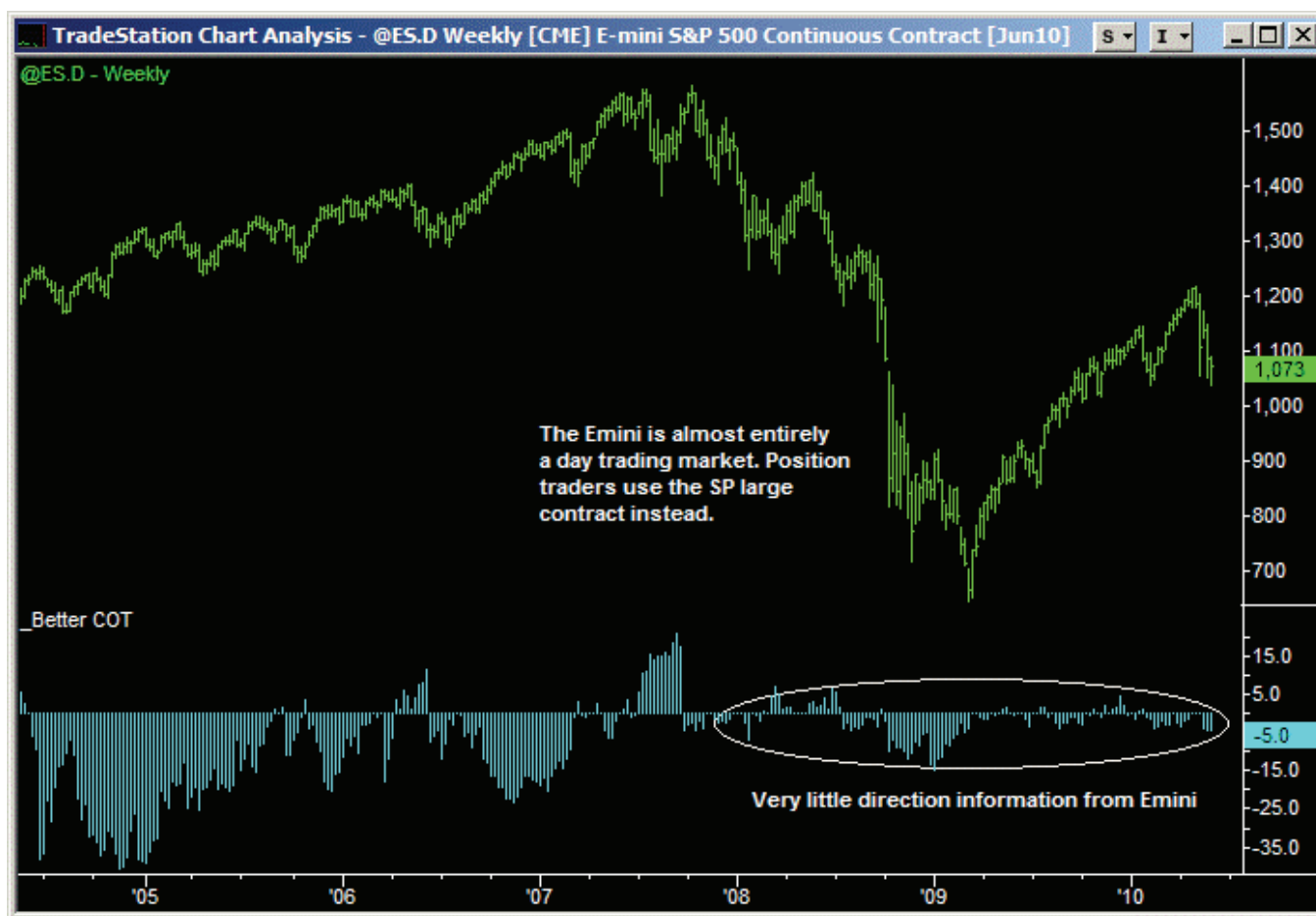
## Commitment of Traders and Emini Trading: My 5 Suggestions

The Commitment of Traders analysis is secondary in my Emini trading. The data is only released weekly and I put more emphasis on price cycles, volume momentum and Professional activity. That being said, the Commitment of Traders data is useful in confirming over-bought/sold levels and identifying potential market turning points.

Here are my suggestions for using Commitment of Traders analysis in Emini trading:

1. Use the SP (full-size) Commitment of Traders data not the ES (Emini)
2. Use an Oscillator to identify over-bought and over-sold levels
3. Keep an eye on the stock market Crash Warning Indicator
4. Follow related markets like Crude Oil and US Treasury Bonds, and
5. Move your trading capital when long term Forex trends change

## 1. Use the SP Commitment of Traders Data not the ES



*Commitment of Traders: Emini Professionals Long/Short (% Open Interest)*

If you're an Emini trader you've got 5 Commitment of Traders data choices:

- Obviously data for the Emini (ES)
- Data for the large S&P500 contract (SP)
- Combined data for all the "mini" contracts (Emini, mini-Dow, mini-NASDAQ, etc.)
- Combined data for all the "full-size" contracts (S&P500, Dow, NASDAQ, etc.)
- Combined data for all the indices

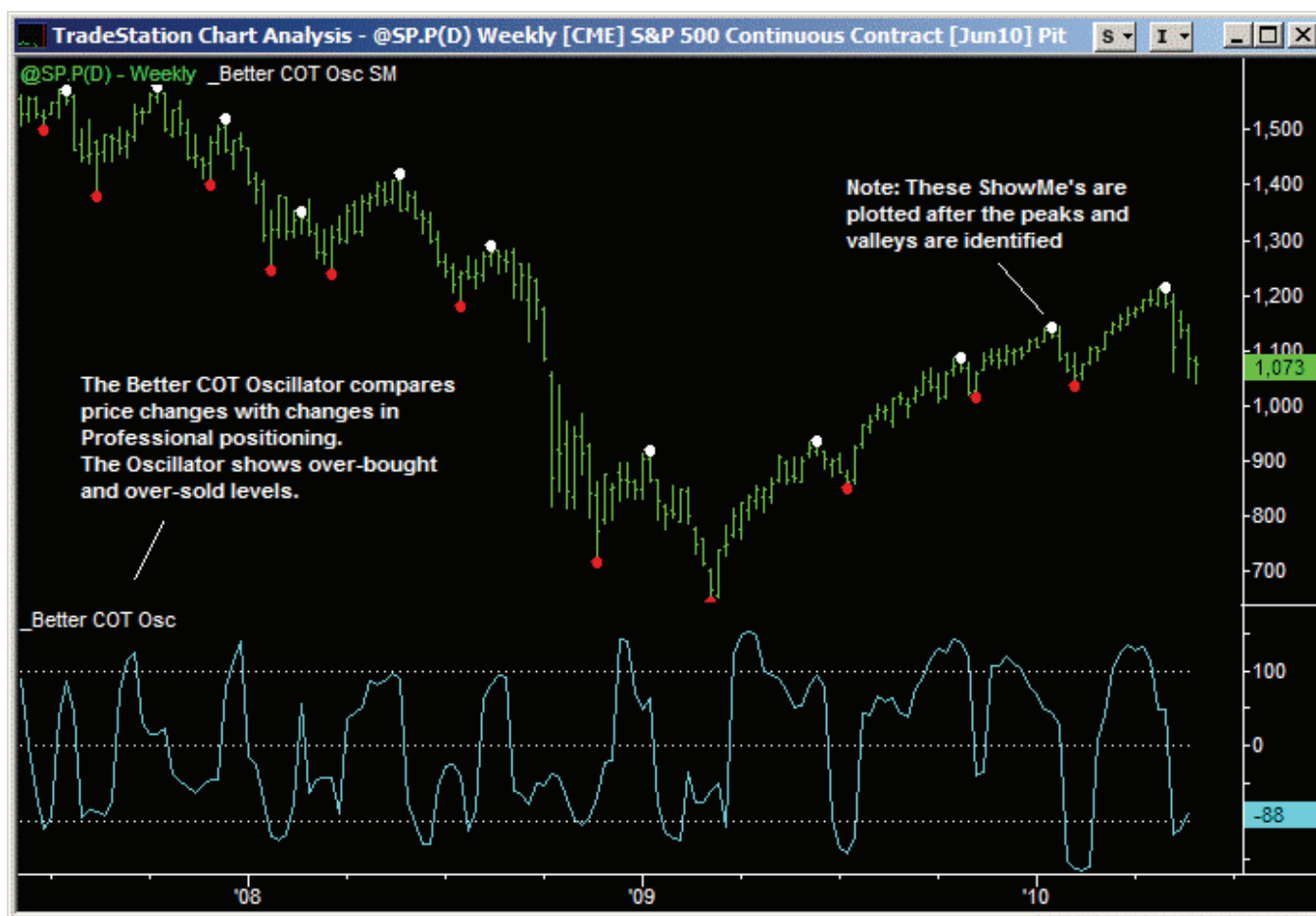
Note: Commitment of Traders data can be combined across different contracts by weighting the Long/Short data by the margin required to trade each different contract.

The chart above shows the directional information from the Emini (ES) contract is very weak, particularly recently. The Professional's Long/Short positioning shows swings that are smaller than the large S&P contract (SP).

In my opinion, this is because the Emini has become almost exclusively a day trading vehicle. Whereas, the large S&P contract is used more for position trading and hedging. The other "mini" and "full-size" contracts show a similar pattern.

As a result, I use the large S&P contract (SP) in my Commitment of Traders analysis and ignore the Emini (ES) data.

## 2. Use an Oscillator to Identify Over-Bought and Over-Sold Levels

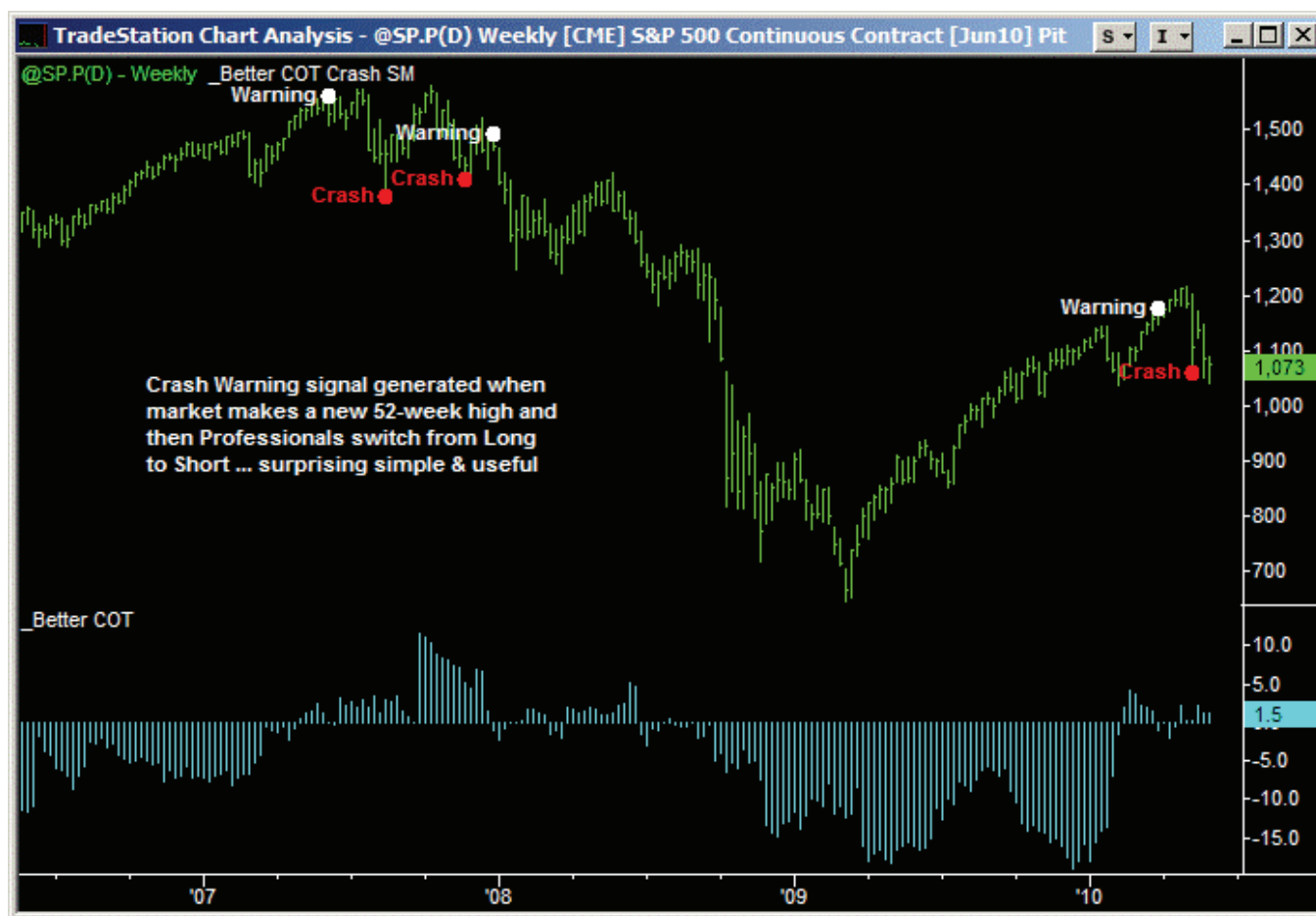


*Commitment of Traders: Better COT Oscillator*

The usefulness of the Commitment of Traders data comes when you combine it with price. I use a clever little algorithm to compare changes in price with changes in the Commitment of Traders data. This generates an Oscillator which shows me when the Professionals consider a market to be over-bought or over-sold.

The chart above shows the Oscillator applied to weekly data for the large S&P contract (SP). As you can see it tracks market swings nicely. The red and white dots on the weekly price bars are superimposed after the Oscillator crosses the zero line to mark the high or low point of each swing.

### 3. Keep an Eye on the Stock Market Crash Warning Indicator



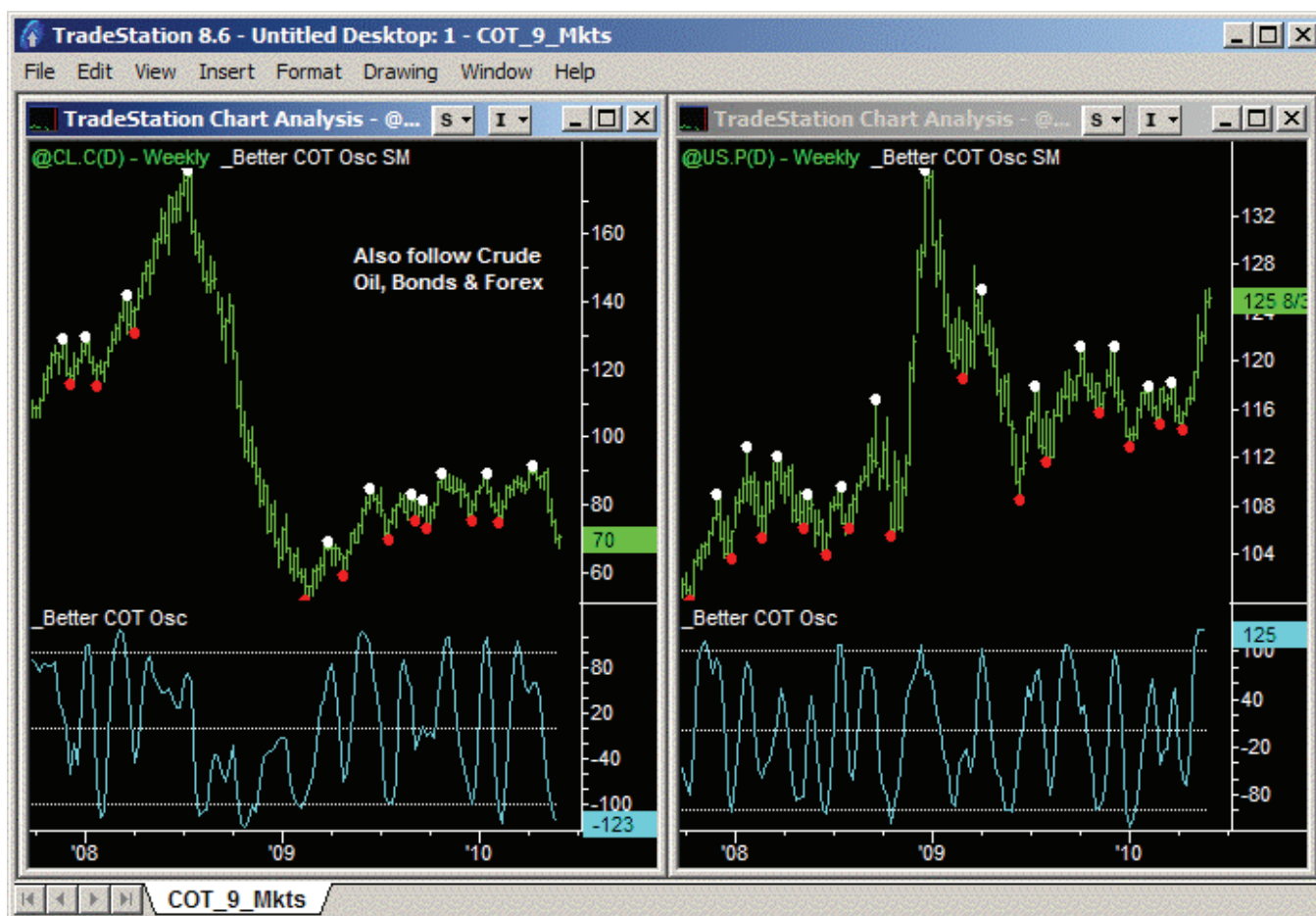
*Commitment of Traders: Stock Market Crashes 2007 – 2010*

The pattern mentioned earlier of Professionals switching to trend following, once a strong trend develops, can be used to create a stock market Crash Warning indicator. For the indicator to signal the following sequence of events needs to take place:

- Stock market makes a new 52 week high while the Commercials are net Long
- The Commercials flip from net Long to net Short
- A "Warning" signal is printed on the chart, and
- The signal is confirmed once the market drops 10% from the high

Simple, but very effective. Check out the chart above that shows the market corrections from 2007 to 2010. Crash Warning signals were generated before each one. If you're interested in seeing more, go to the bottom of this page and follow the link to see similar signals for 1987, 1997, 1998 and 2000.

## 4. Follow Related Markets Like Crude Oil and US Treasury Bonds



*Commitment of Traders: Better COT Oscillator for Crude Oil and Bonds*

Now that the Commitment of Traders data is accessible within TradeStation, it's easy to apply the Better COT Oscillator to other markets. From an Emini trading perspective, the most important markets to follow are Crude Oil and US Treasury Bonds.

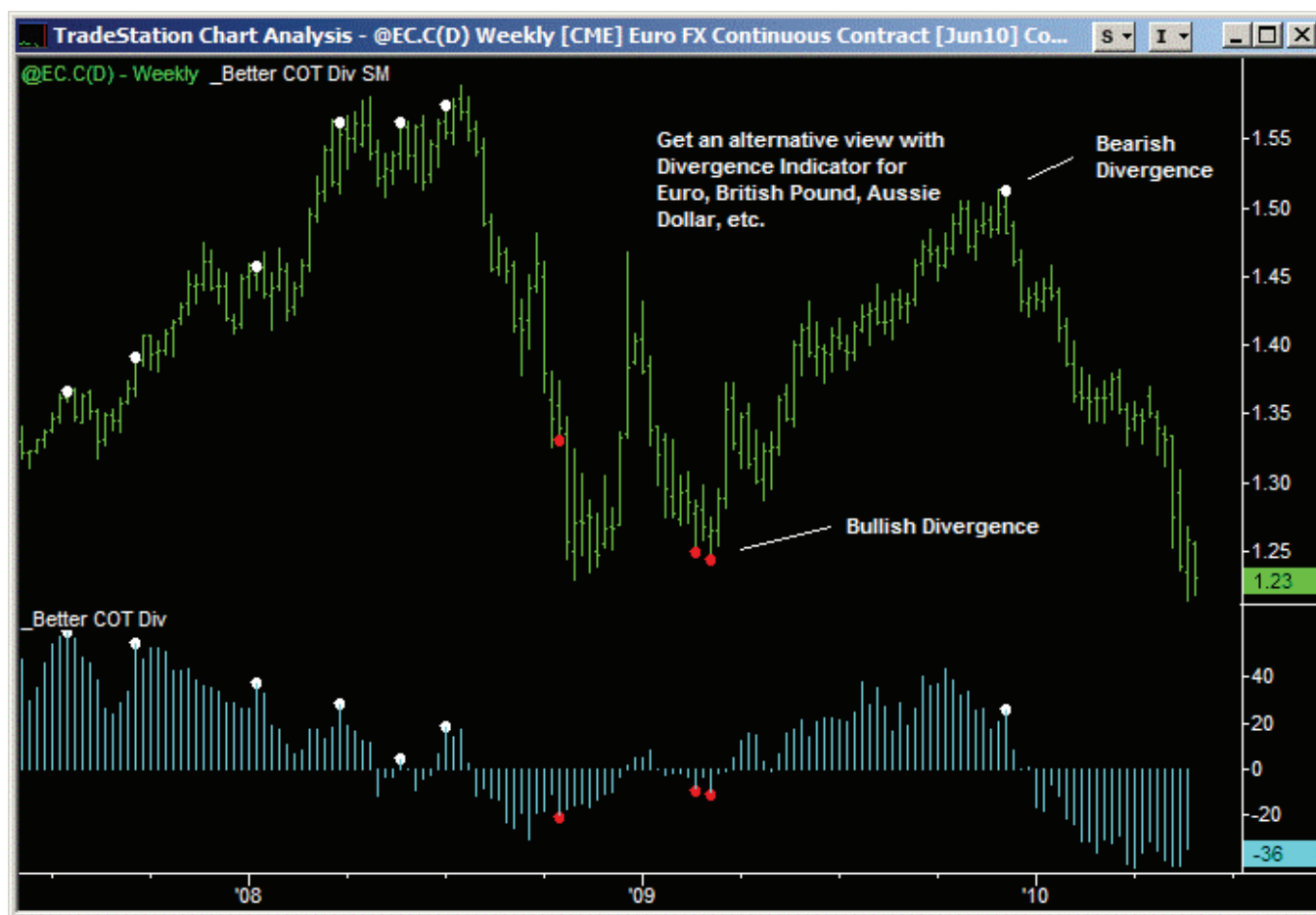
Crude Oil is a proxy for global growth and global growth results in corporate profits and rising stock markets. So the stock market and Crude Oil are directly correlated.

The relationship between the Bond and stock markets is more complex. Sometimes they are directly correlated and sometimes they are not. When investment prospects are good, capital flows into both equities and Bonds and they'll both rise together.

However, when perceived risks are high, investors will prefer Bonds over equities. Nonetheless, turning points in the Bond market often lead the stock market and so the Bond market is worth following.

The chart above shows the Better COT Oscillator on both Crude Oil and Bonds.

## 5. Move Your Trading Capital When Long Term Forex Trends Change



*Commitment of Traders: Euro and Divergence Patterns*

Lastly, I don't trade Forex because volume data is not available and there are too many currency pairs to track. However, I don't want to keep my trading capital in a weak currency. Once or maybe twice a year I move my trading capital into what I perceive to be the strongest currency. Investment professionals call this a "currency overlay".

For that reason I keep an eye on the major currencies: US Dollar, Euro, British Pound, Japanese Yen and Australian Dollar. When I see major shifts, for example into or out of the US Dollar, I move my capital accordingly.

The chart above shows a useful Divergence indicator that compares the Commitment of Traders data with the underlying futures market. The indicator is based on the Better Momentum divergence algorithm but is still a work in progress. (Note the Commitment of Traders data has been inverted.)

## What People Are Saying About the Commitment of Traders Oscillator

"I tested all the different combinations and found that your method of futures only, all large contracts and net % had the best profit factor. I was really impressed because this tested better than Steve Briese's method and he is known as "the" COT expert. **Your COT Oscillator is so simple, it's ingenious!**" Michael M.

I publish the updated Commitment of Traders charts every week. Make sure you [subscribe](#) to the free website updates. For more information check out these links:

- [Commitment of Traders – Do Professionals Hedge or Trend Follow?](#)
- [Commitment of Traders – Importing Data into TradeStation](#)
- [Commitment of Traders – Should You Use ES or SP Data?](#)
- [Commitment of Traders – Stock Market Crash Indicator](#)
- [Commitment of Traders – Archive of Weekly Updates](#)

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