Non-Commercial Positions And Commodity Index Levels

Whenever people ask me whether the weekly Commitments of Traders report from the Commodity Futures Trading Commission is useless or worthless, I offer the response, “Both.” This is not to say you will not find some examples of an egregiously out-of-balance long (short) position in futures followed by some sort of selloff (rally) afterwards, but a small collection of anecdotes doth not a hypothesis make.

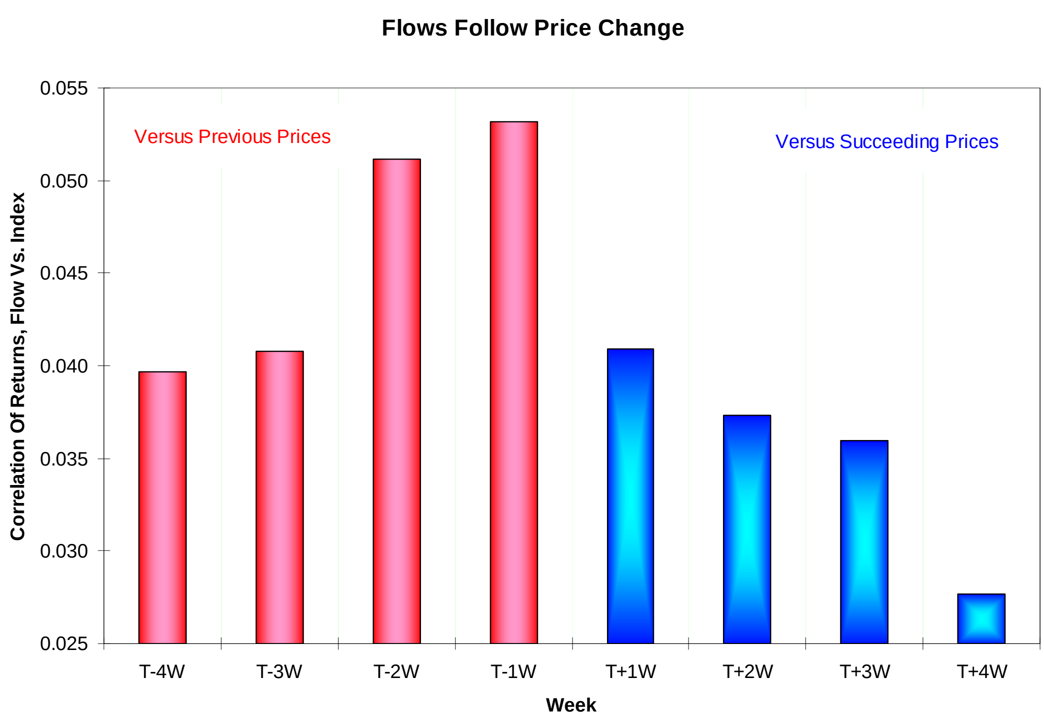
What would be required for such a hypothesis to be valid? Let’s start with a demonstrable leading position between net trader positions leading price movements regularly and reliably across a complete cross-section of markets. To keep a long story short, I have examined the net positions for two classes of traders, Managed Money and what the CFTC poetically describes as “Other Reportables” over the set of physical commodities and have found such a relationship lacking, completely and utterly. Slam the door, stick a fork in it, bring in the proverbial Fat Lady to belt out a tune or two; the relationships are not there.

The CFTC only began collecting data for these expanded categories in 2006, but it has been collecting data for so-called commercial and non-commercial traders since 1992. This division is based on the amusing supposition commercial traders are more likely to be hedgers rather than speculators and – here’s the real knee-slapper – have greater understanding of their markets than those who must get markets right or get out of the trading business if they fail to do so. This worldview might have hedgers wear white in homage to the brides who do so to symbolize their virtue.

A Simple Test

I would like to tell you bad ideas can be slain by good analysis, but experience has taught me willful ignorance will outlive the Egyptian pyramids. But let’s have a go, anyway. The net non-commercial positions for the seventeen American-traded components of the Continuous Commodity index (CCI) and the weekly geometric average of that index were used to construct a weekly money-flow series.

This was correlated against CCI price returns over the previous four, three, two and one weeks. All data have been adjusted to account for the gap between the Tuesday reporting period and the Friday release of the CFTC data. A correlelogram for these flows’ weekly returns against CCI price returns over the next one, two, three and four weeks can be constructed. While the causal relationship is not strong, its relative direction is clear: CCI prices determine money-flows by non-commercial traders, not vice-versa. This makes absolute intuitive sense: As most non-commercial traders are trend-followers of one form or another, we should expect their positions to follow, and not to determine prices.



Can these net positions lead price at all? The sum of these seventeen net non-commercial positions leads the weekly geometric average of the CCI index by seven weeks on average. This implies changes in net trader position have no immediate effect or plausible short-term effect, but rather an almost two month-ahead effect (r^2=0.80).

Few experienced traders have witnessed this delayed reaction between net non-commercial positions and price and for good reason: The proposition net non-commercial positions lead price remains non-demonstrable.

Non-Commercial Positions Lead Price By 7 Weeks