

Crowded Market Report

April 16th 2023

By Jason Shapiro

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Contents

Things to keep in mind.....	3
Equities.....	4
Fixed Income	7
Currencies	9
Energies.....	11
Metals	13
Softs	16
Livestock.....	17
Crypto Currencies	18
Putting it All Together... ..	19
Current Positions	20
Last Week's Trades	20
Appendix	21
Week over Week Heat Map.....	21
Overall Market – Sorted by Commercials.....	22
Overall Market – Sorted by Large Speculator.....	23
Overall Market – Sorted by Small Speculator	24
Sectors.....	25
Currencies	25
Energies.....	25
Equities.....	26
Fixed Income	26
Grains	27
Livestock.....	27
Metals	28
Softs	28

Things to keep in mind...

We highly recommend that newer members start with reading the [New Member Guide](#).

The COT Report data is released by the CFTC each Friday after the market close and measures Futures positions as of close. In other words, the data is three days old when published. The CFTC data includes market participation by several types of traders, and it can be viewed as a sentiment indicator based on actual positions versus opinion in a survey. Participants include Commercial Hedgers, Large Speculators, Small Speculators. Commercial Hedgers essentially created the commodity Futures markets and control majority of the open interest. A classic example of Commercials is Gold Producers/Miners. In more recent years, commodity index funds became non-traditional Commercials, as index funds gained popularity. Large Speculators may include hedge funds (ironic since Commercials are actually hedging and “hedge” funds are speculating) and their participant number may match the number of Commercials, but their position size will be much Smaller. Lastly, we have Small Speculators which is essentially Open Interest minus Commercials and Large Speculators. Essentially Small Speculators are those that do not meet the criteria of being Large Speculator as reported to the CFTC.

As far as assessing the COT data, my process is to review current market participation against historical levels. I am not looking at absolute levels (ex. Commercials being net short or long) but rather relative levels based on historical levels (ex. how are Commercials currently positioned compared to a specified time frame. Unfortunately, I cannot share more details as that is part of my proprietary process. Let us work through an example to better clarify this process. We will continue with the Gold theme. Commercials are always going to be sellers as hedgers are Gold producers and they need to sell what they produce. If I was using absolute levels, it would be difficult to long Gold since Commercials would indicate they are bearish on Gold, but if I compare their market participation compared to historical data, along with additional insight from how Large and Small Speculators are positioned, then I am able to have market participation confirmation once my COT Index shows the Commercials are “long” Gold since their net short position is low, which means supply is low, which means that additional demand would cause price to go higher.

These indicators of crowdedness do not necessarily mean a market is going to reverse, but rather one piece of the puzzle where a crowded market does in fact reverse, there is potential for a Larger move the other way because there are traders caught on the side that will need to be stopped out. In other words, both market participation and market action would be needed for the move to occur. Market action confirmation would ideally be a news failure event (ex. bullish news, down price action), reversal candle of the highs or lows or correlation failure (ex. Crude Oil up on the day and so is the Yen, which is historically negatively correlated, so it should be down for the day).

While these indicators measure crowdedness relative to history, there can be circumstances where the fundamentals are so strong that the current situation can run further, and therefore create even more crowdedness than we have seen historically. That is why market participation requires market action before a trade is placed. The level of crowdedness in each market is indexed from 0 to 100, with 100 being the largest reading for participants being crowded to the long side and 0 being the Largest crowded reading to the short side. A reading 95 or above confirms the market is crowded long, and a reading 5 or less confirms the market is crowded to the short side. The weekly index data is included in this report and found in the appendix for the markets that are covered.

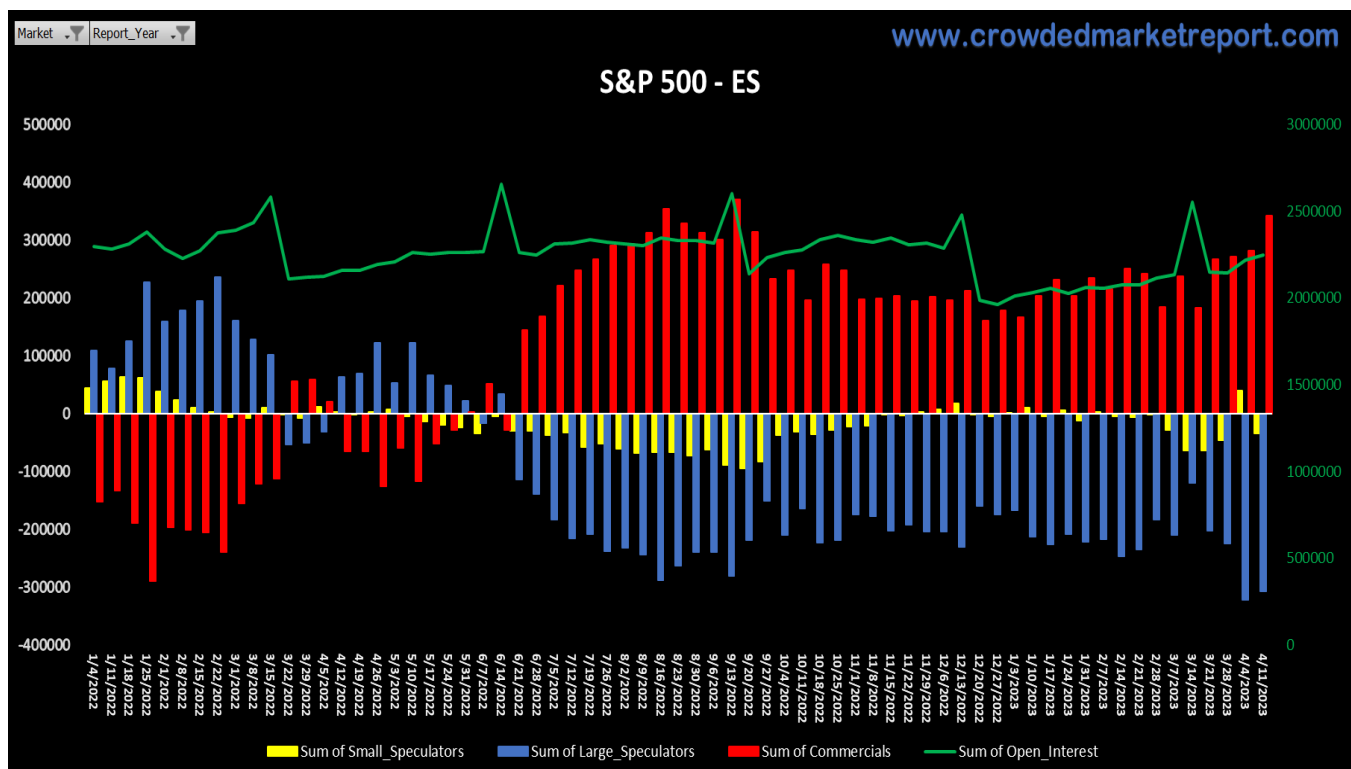
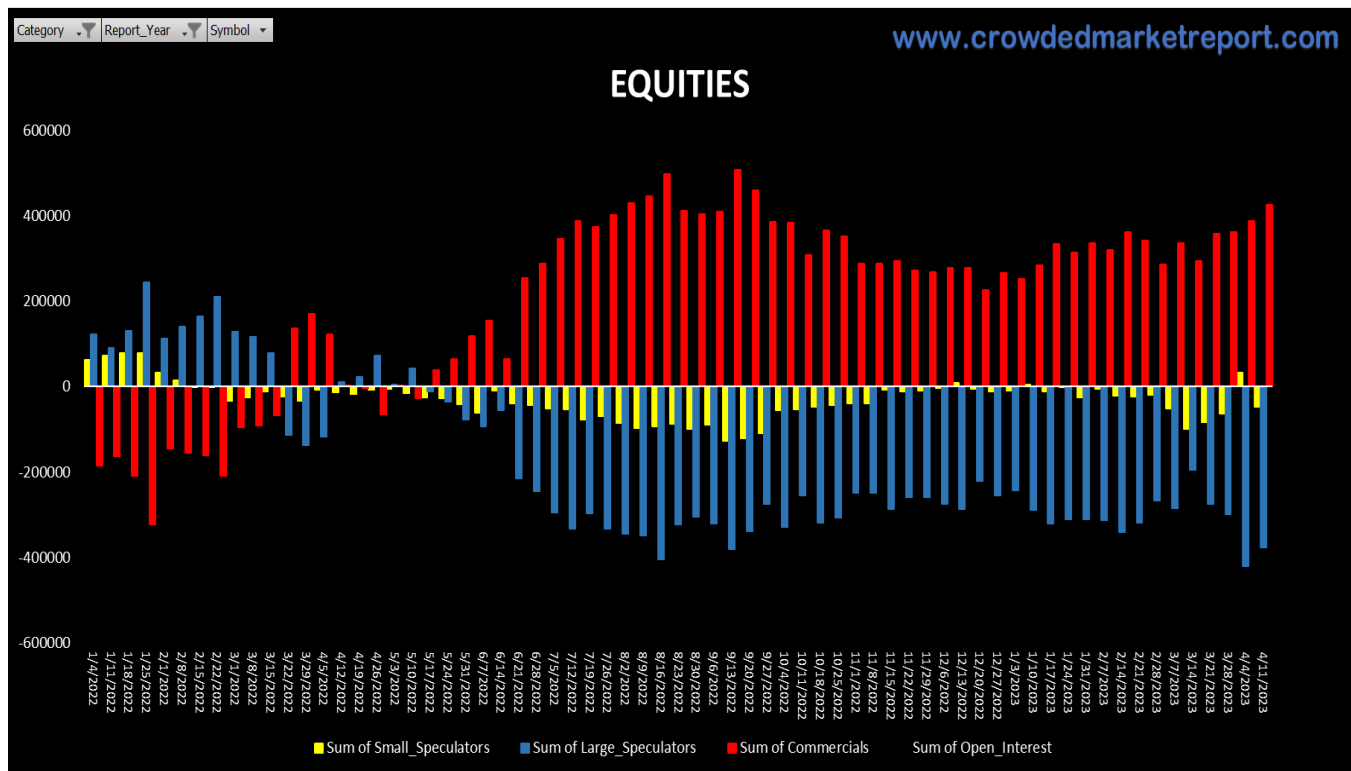
(Short) 0 ←————→ 100 (Long)

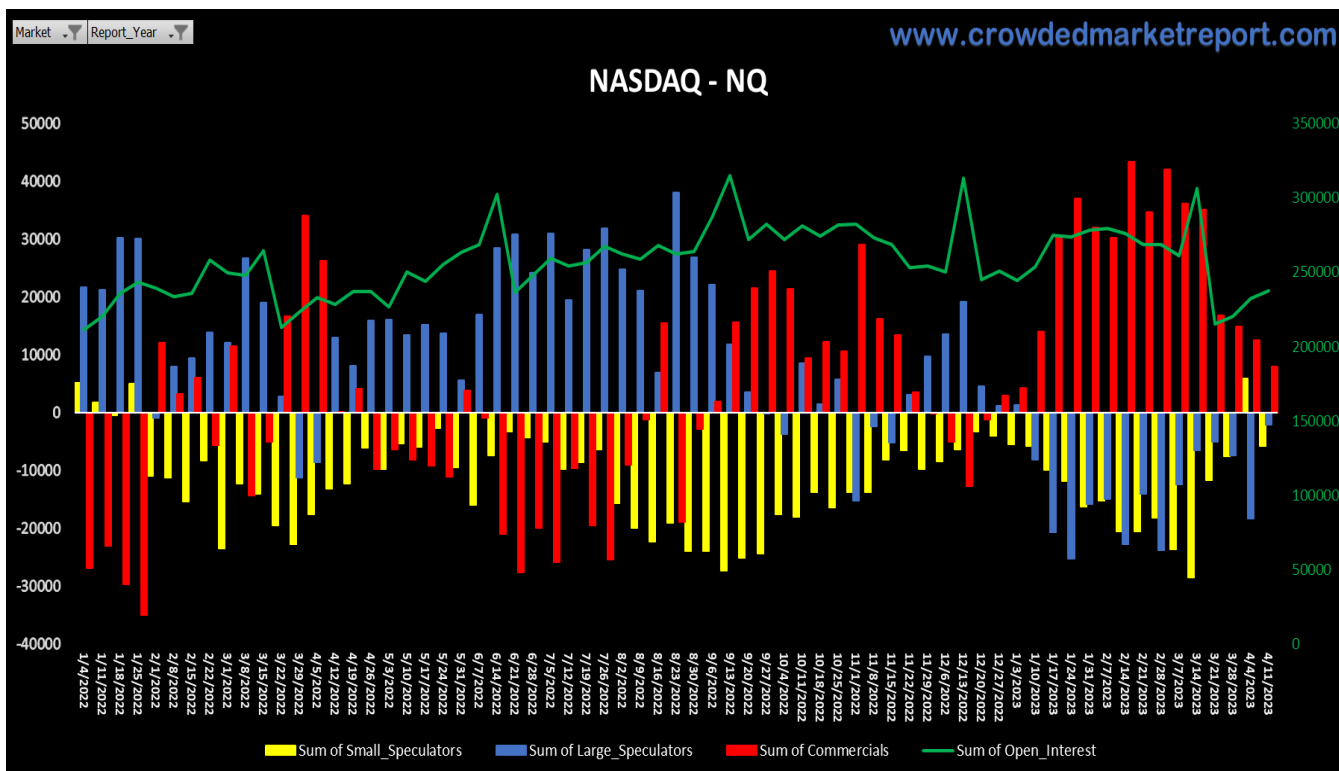
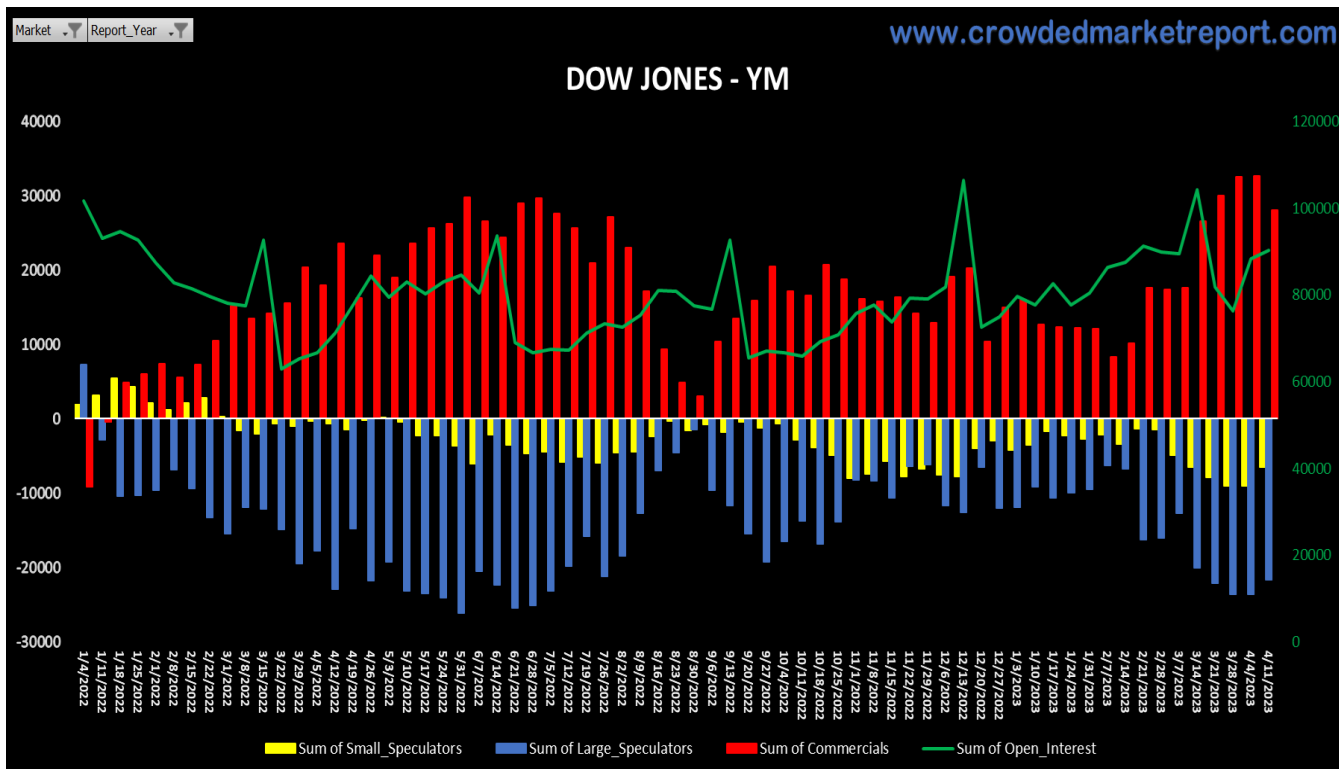
The way I trade these signals is that once a market shows extreme crowded conditions, I am looking to fade the Speculator crowd, but I do not take the trade until the market gives a sign that the trend has potentially run its course. Typically, what I like to see is news to come out that supports the trend, but the market fails to follow through on the news. In other words, should a market be very crowded to the long side and positive news is released, I will sell if the market fails to rally on this news. This is a great indication that the market is bought out or no more buyers are in the market. Of course, the reverse is true for markets crowded short. While this covers most of my trading process, I also consider the longer-term COT chart (~5 Years) to confirm if risk/reward potential remains the same or becomes less attractive when looking at the longer-term charts.

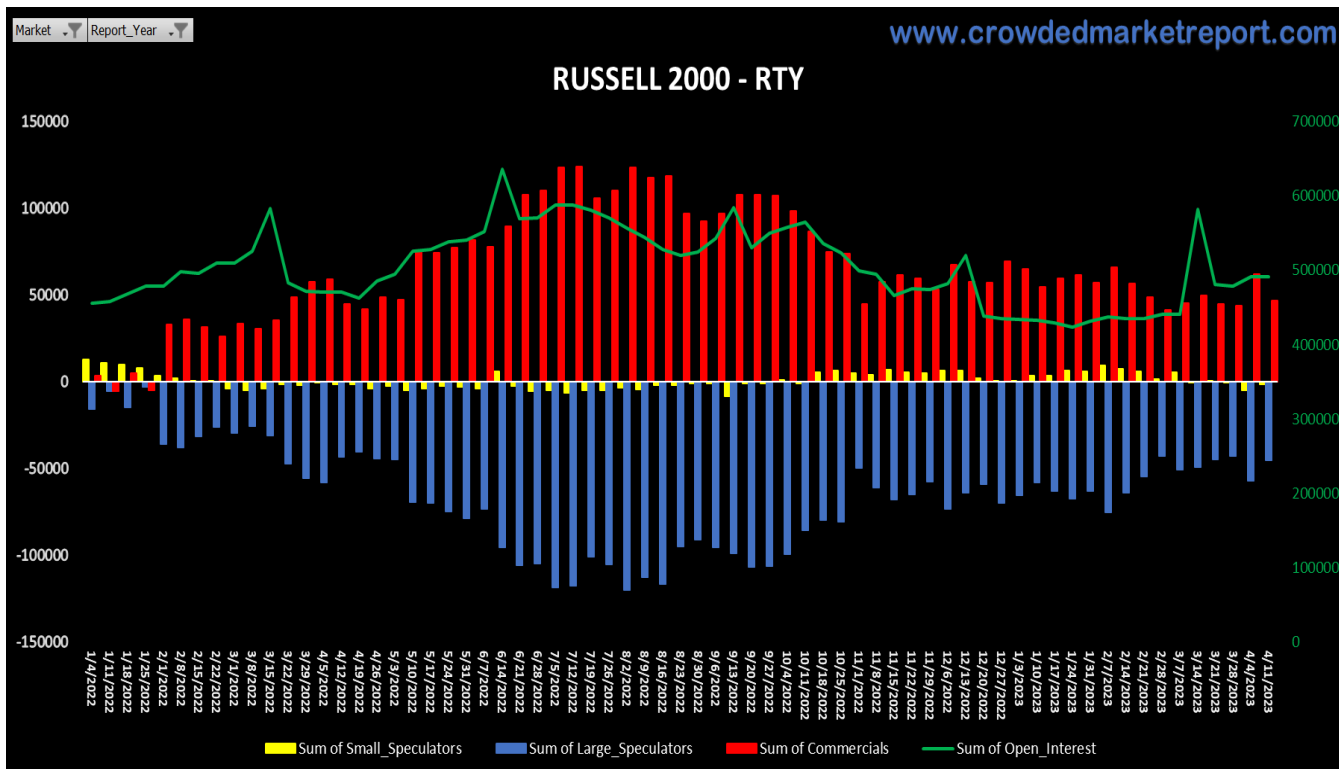
With that in mind, here is a look at each sector...

Equities

While we see some Speculator buying in Nasdaq, Russell, and Dow, it is being matched by Speculator selling in S&P. In keeping with the theme of wanting to be long where Speculators are the most short, I have switched from long Dow to long S&P:

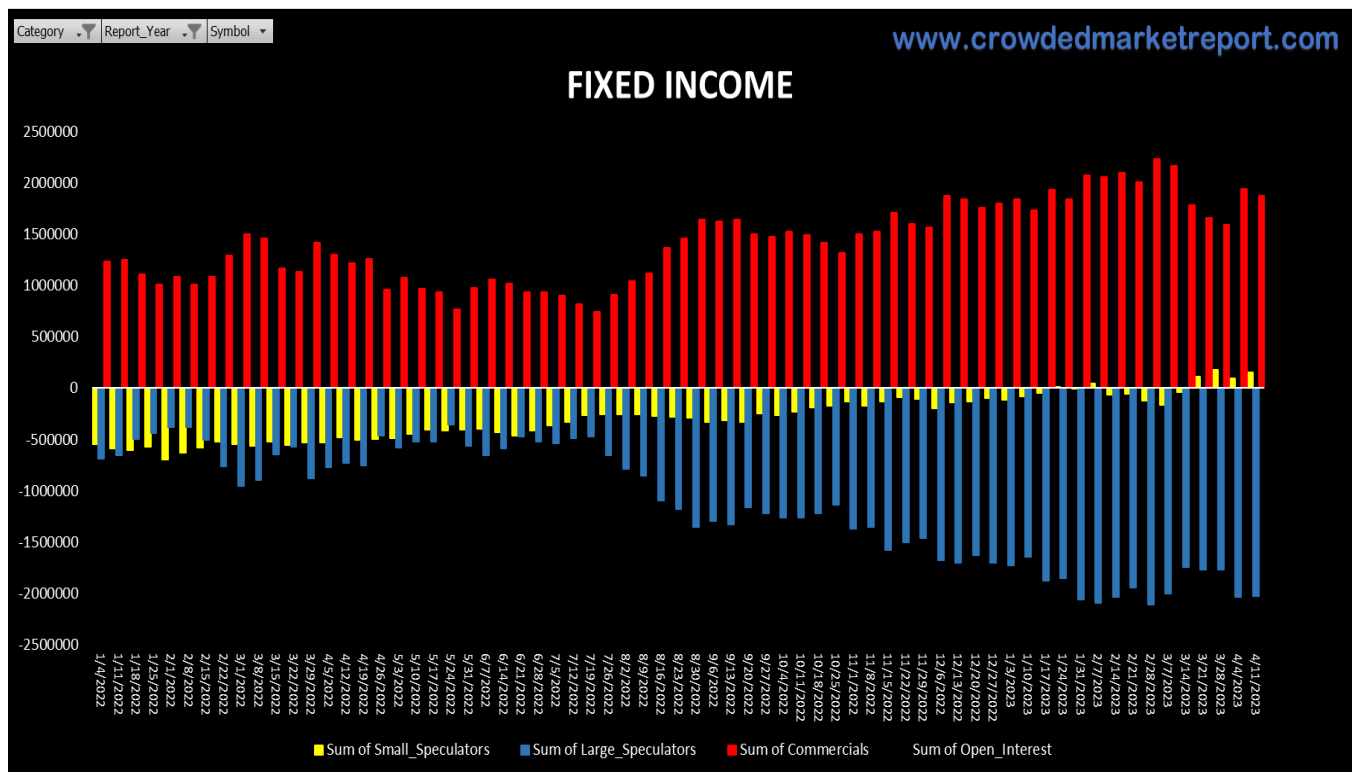




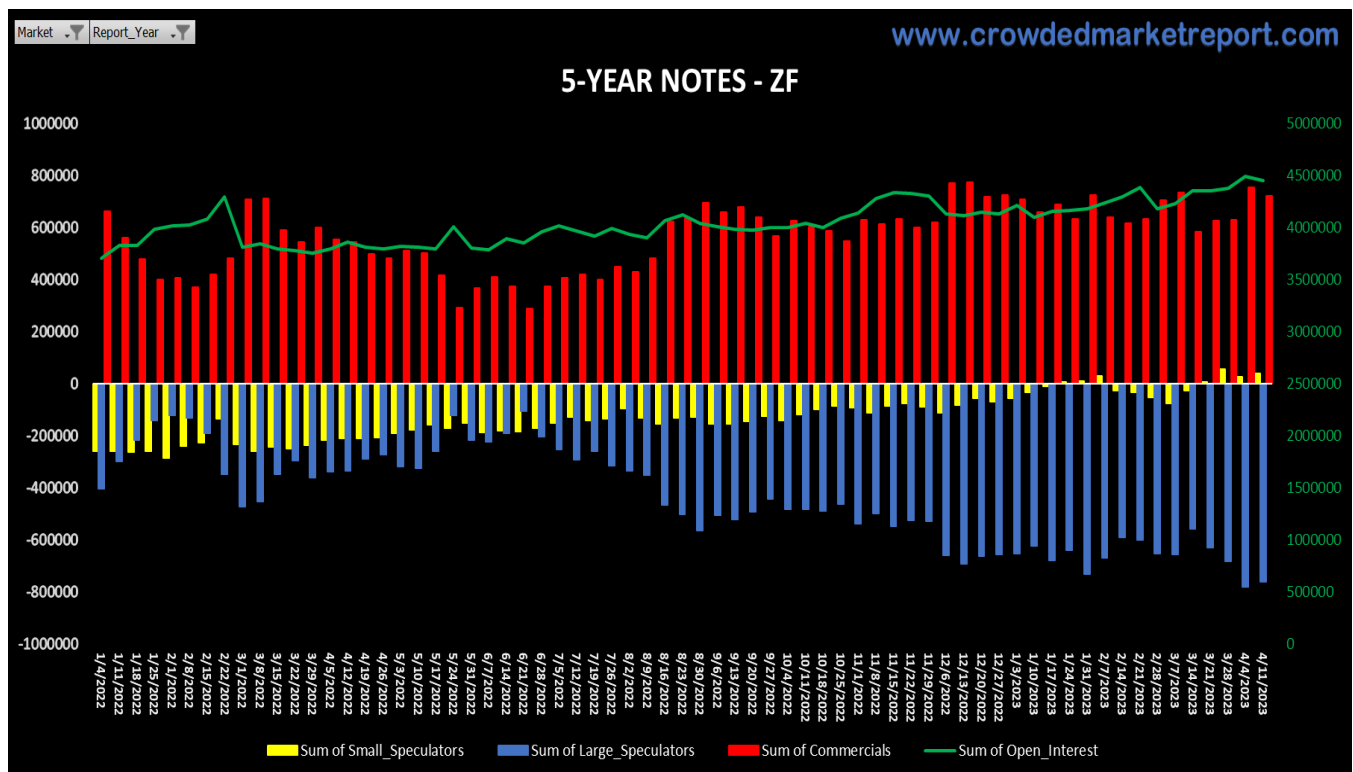


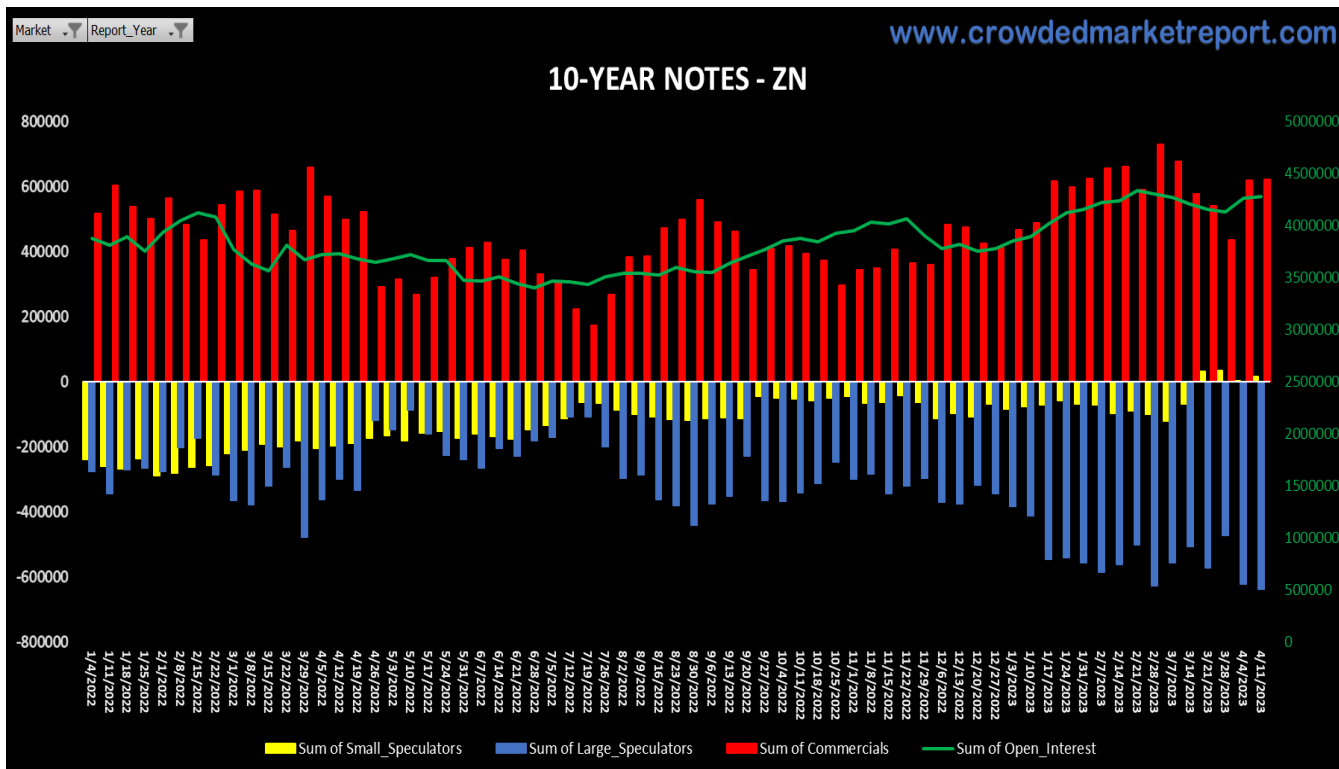
Fixed Income

We continue to find Large Speculators very short Fixed Income:



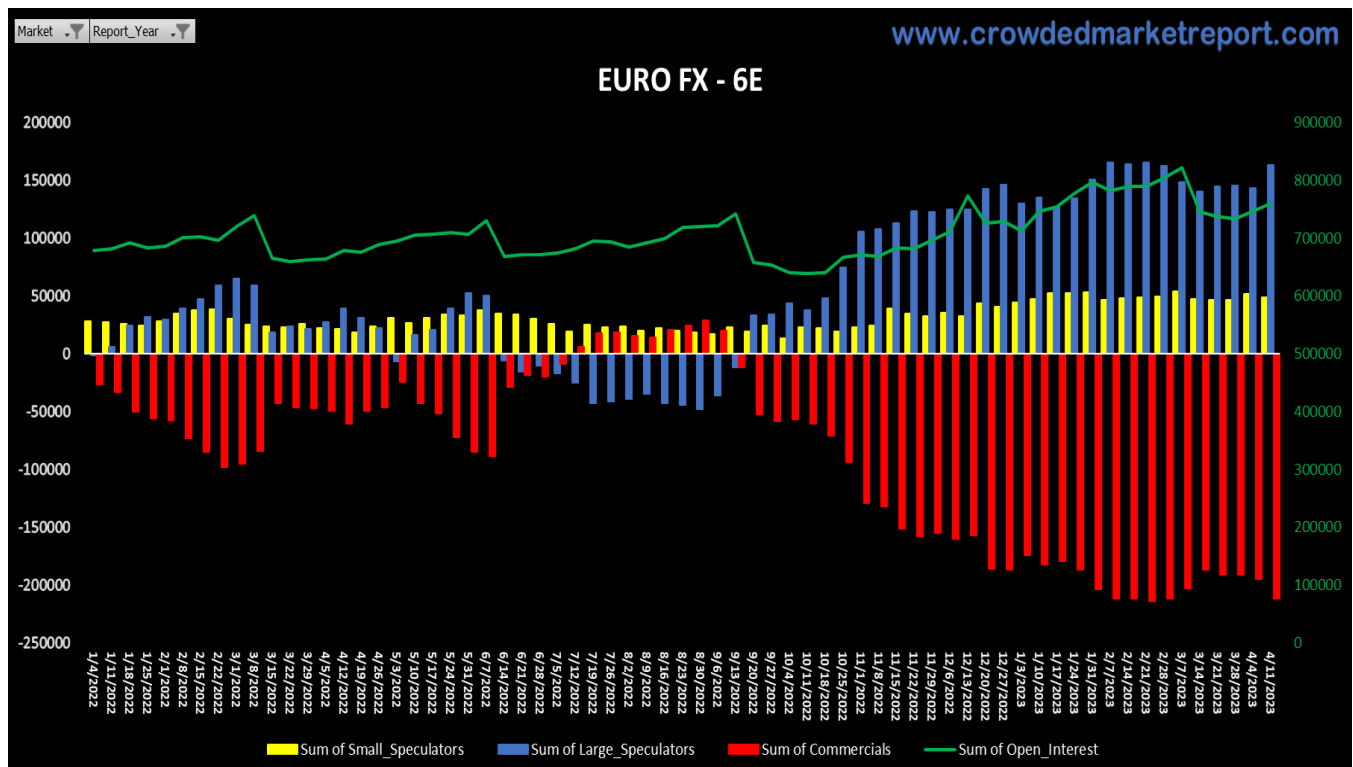
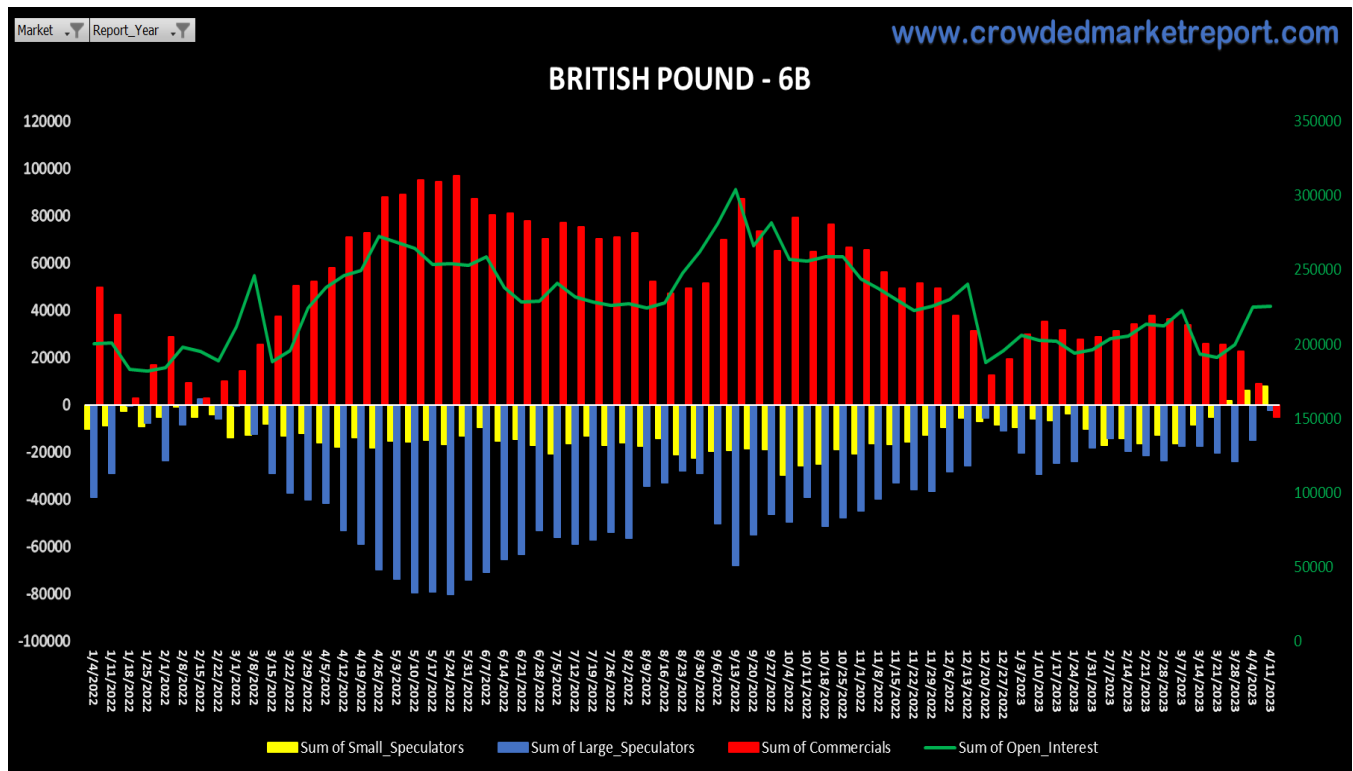
Which is centered mostly around short positioning in 5- and 10-Year Notes:



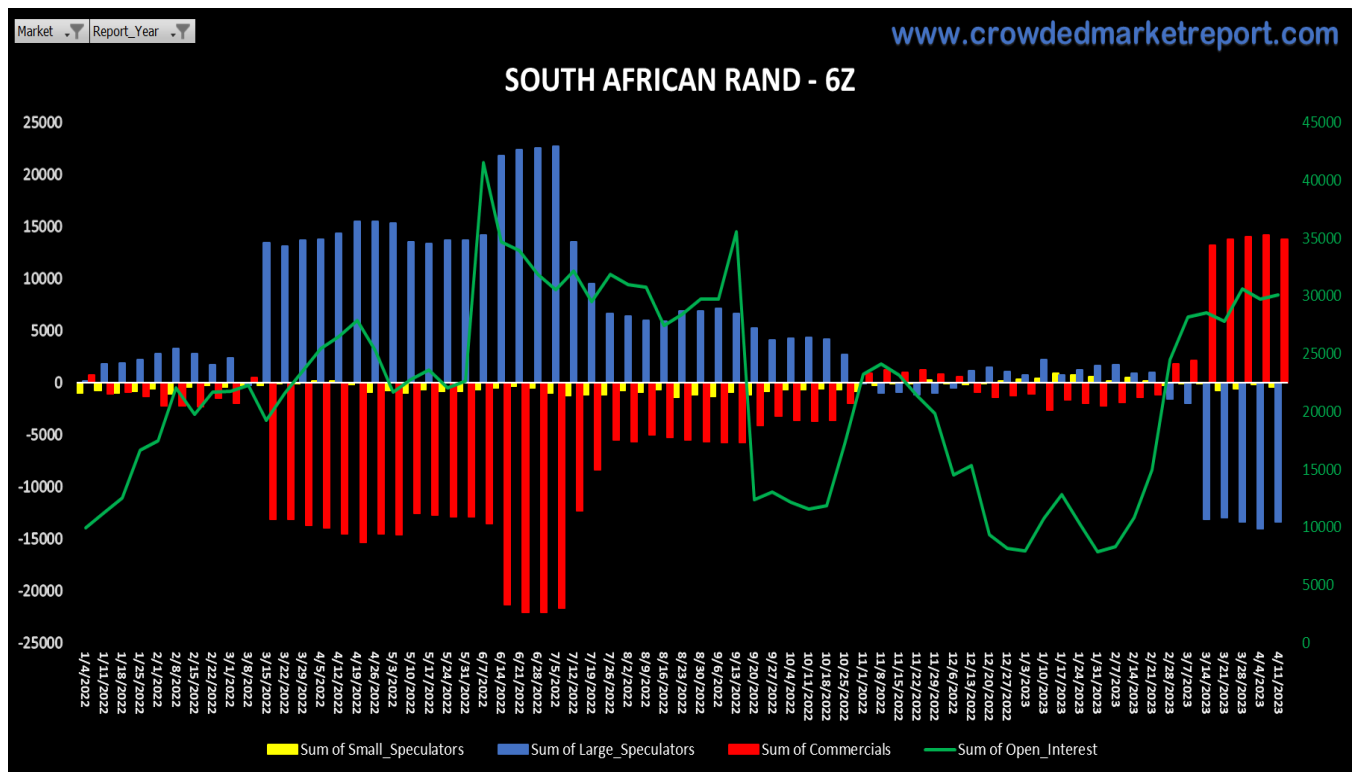
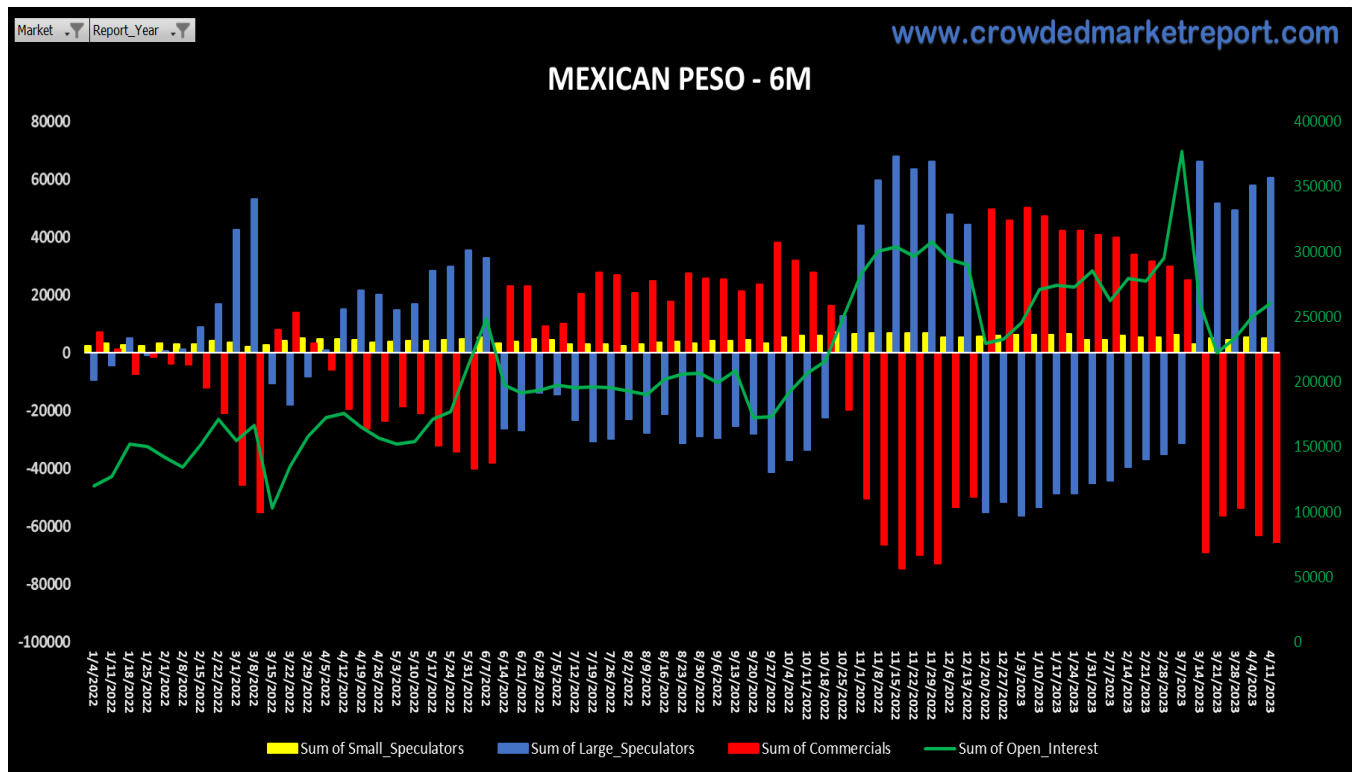


Currencies

There seems to be a lot of “*Death of the US Dollar*” talk going around recently. It was only a few months ago that King Dollar was the talk. If looking to be long USD here, COT would indicate the currencies to be short are British Pound and Euro:

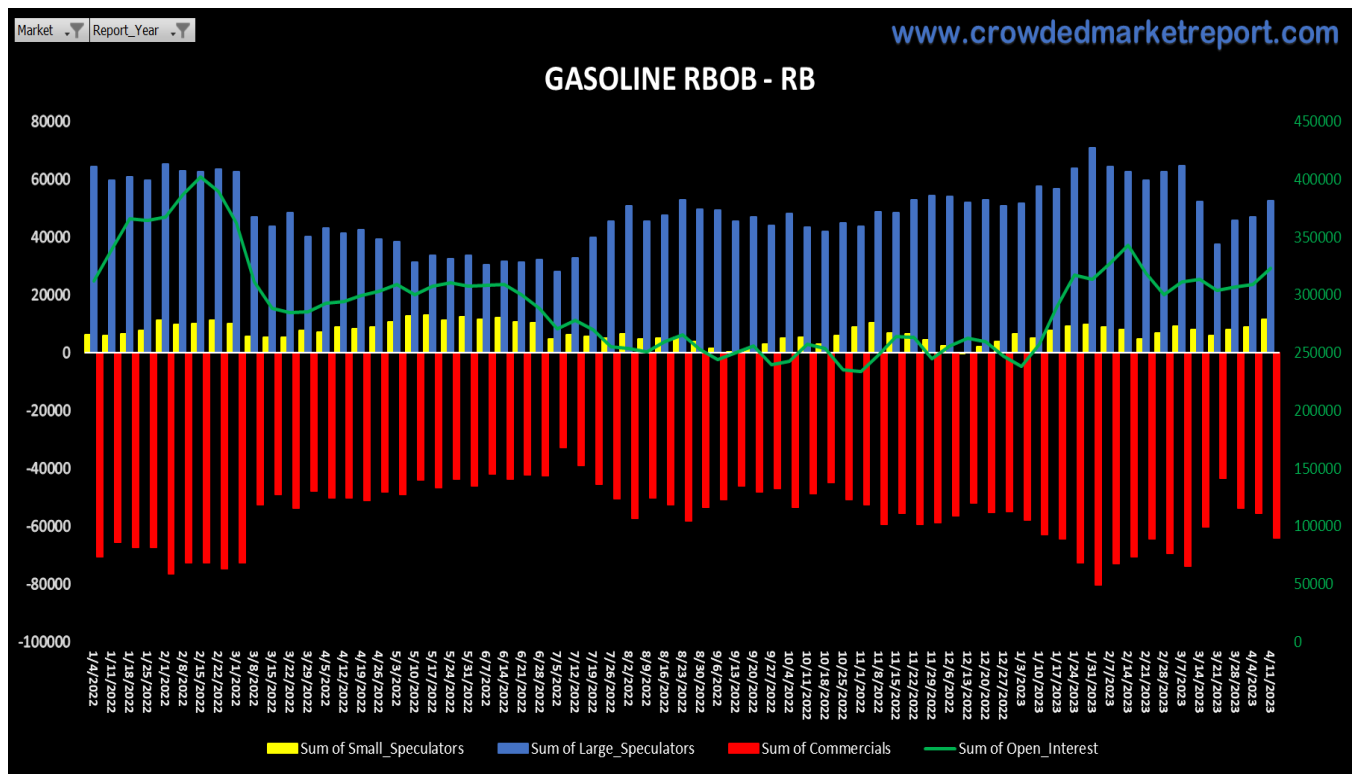
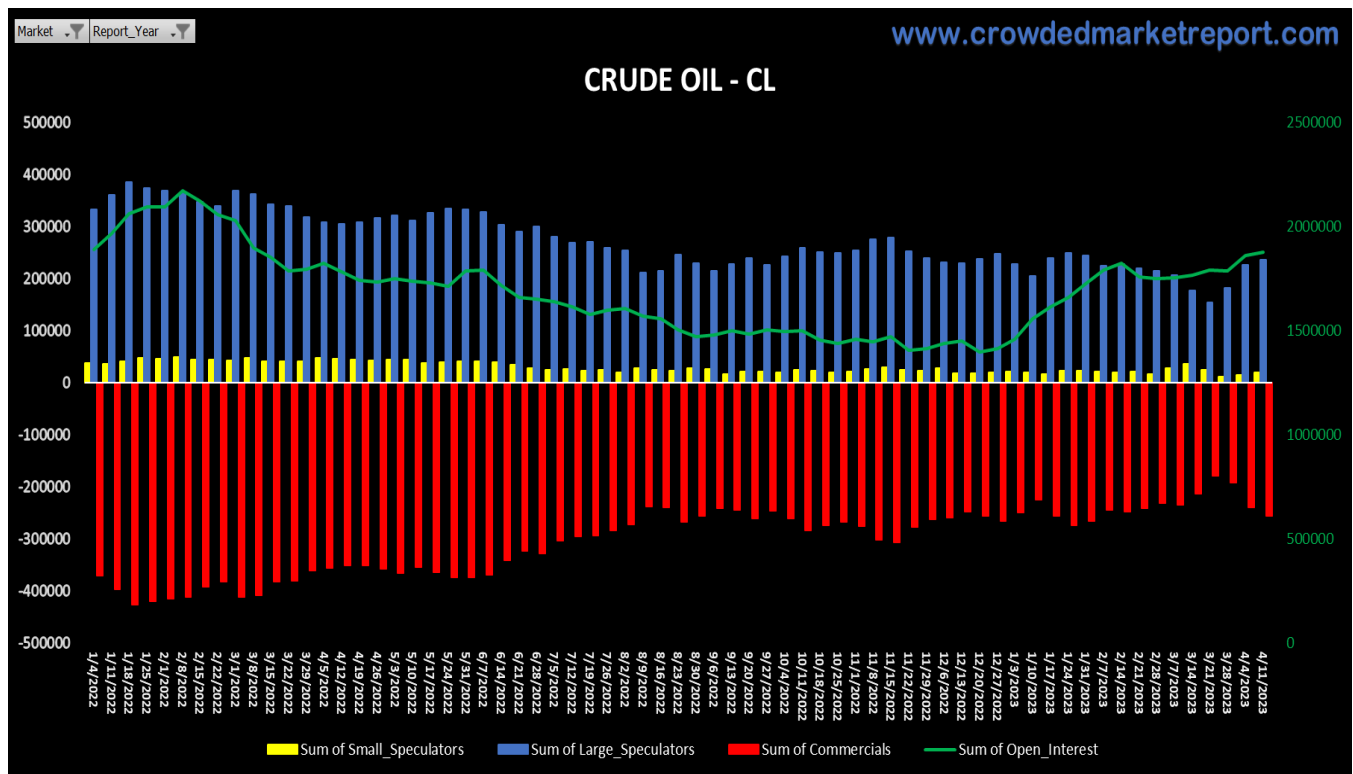


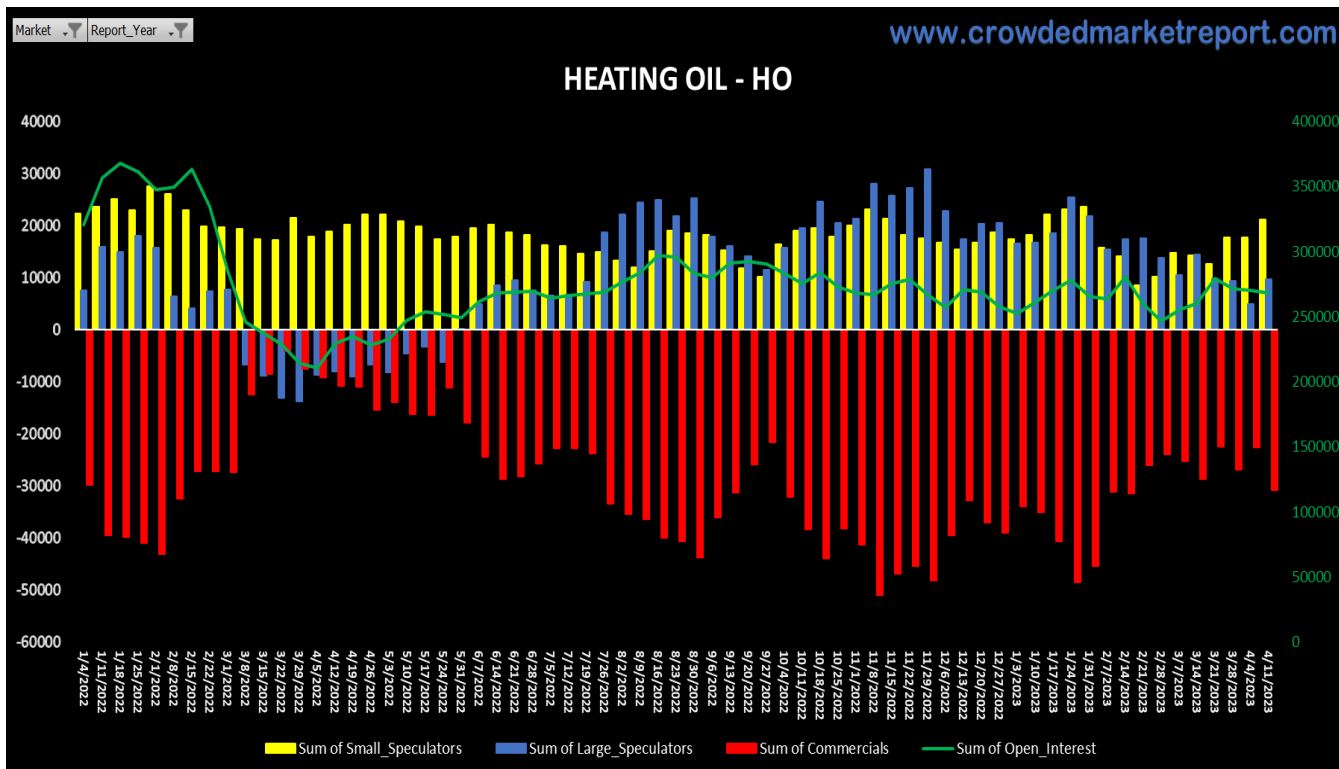
Speculators continue to be quite long Mexican Peso and quite short the South African Rand:



Energies

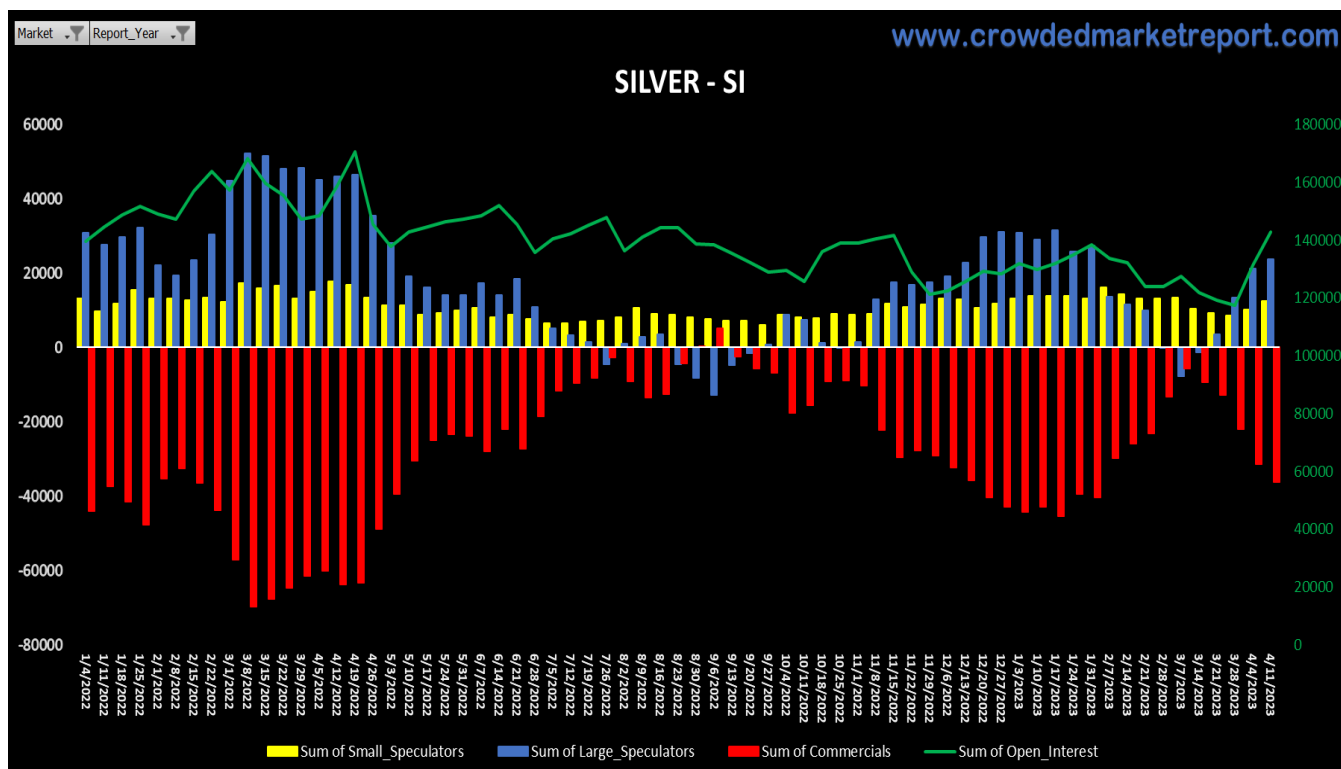
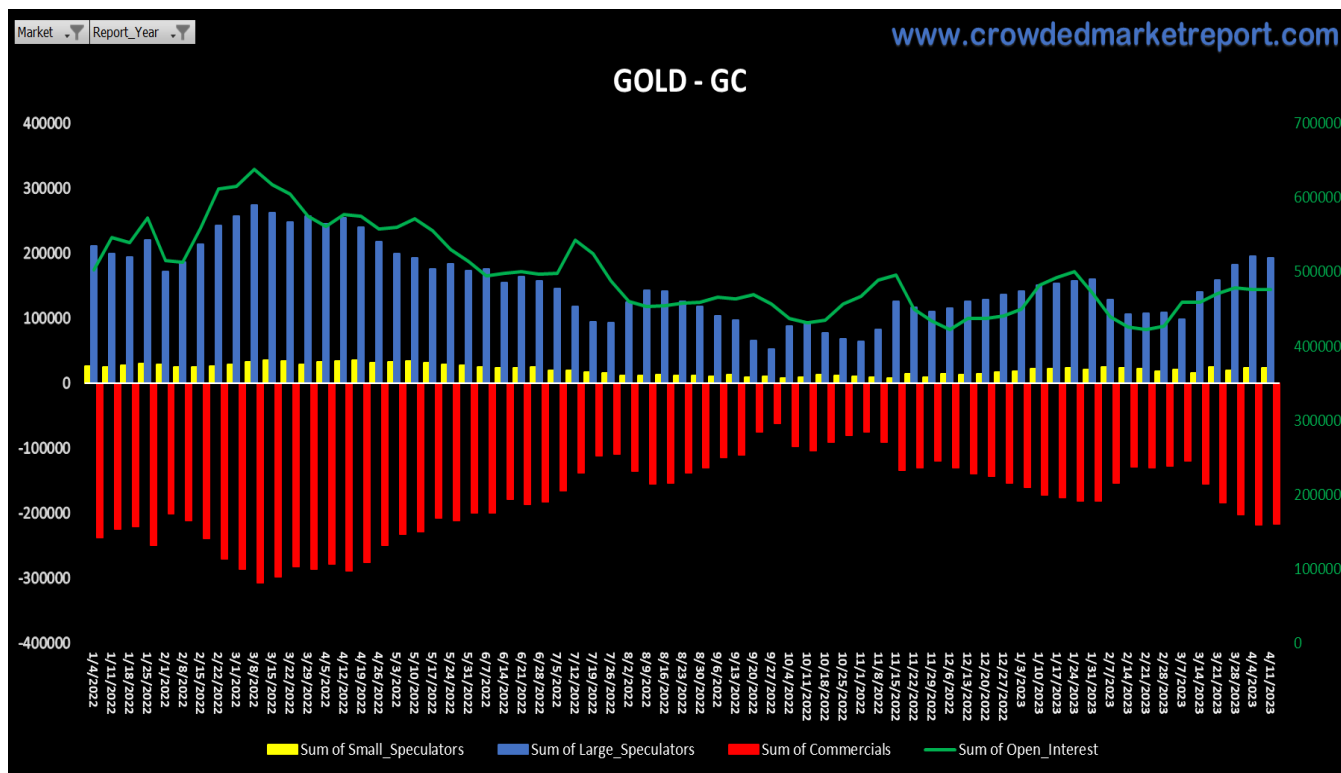
The recent move up in Energies finds Speculators buying Crude Oil, Gasoline and Heating Oil:



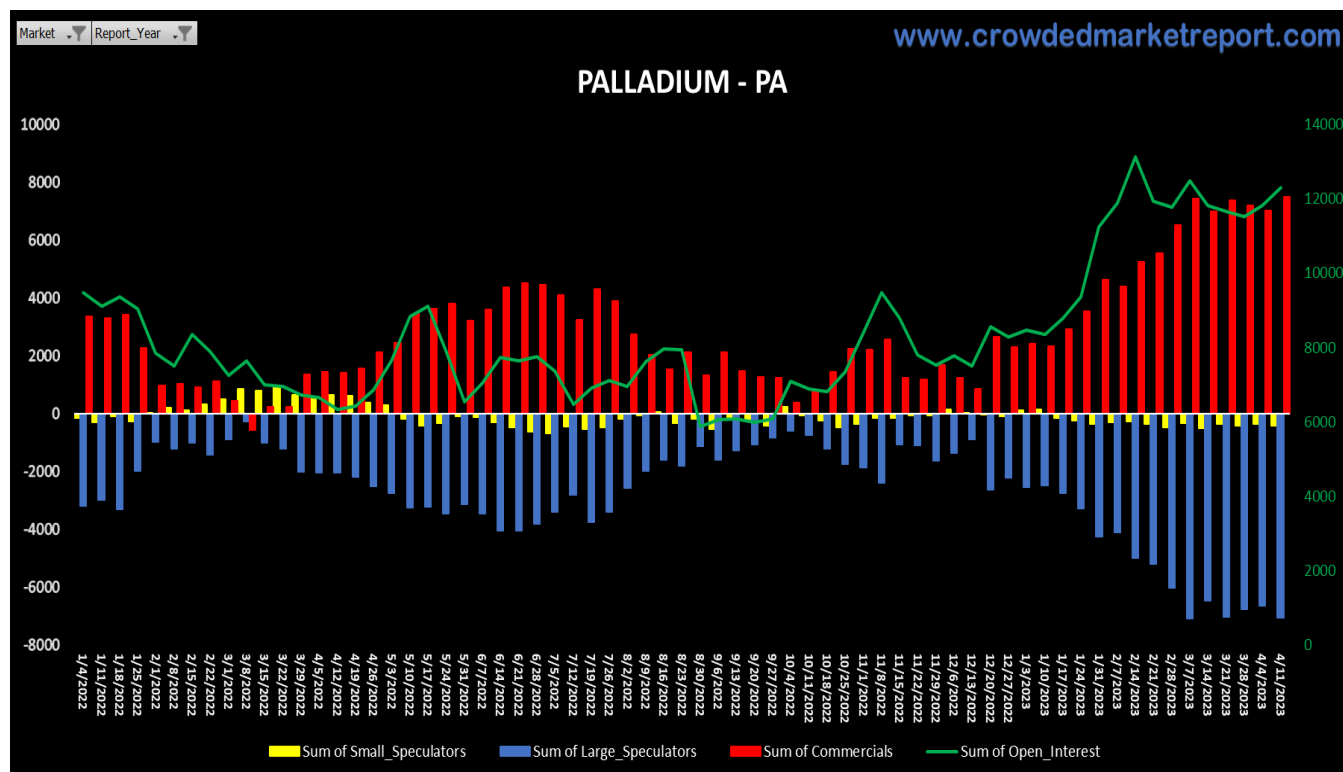


Metals

Gold did a wonderful job of stopping me out again on Thursday just before it had a nice down day on Friday. We did not really see Speculators adding longs into Tuesday, although we are starting to see more Speculator interest on the long side of Silver:

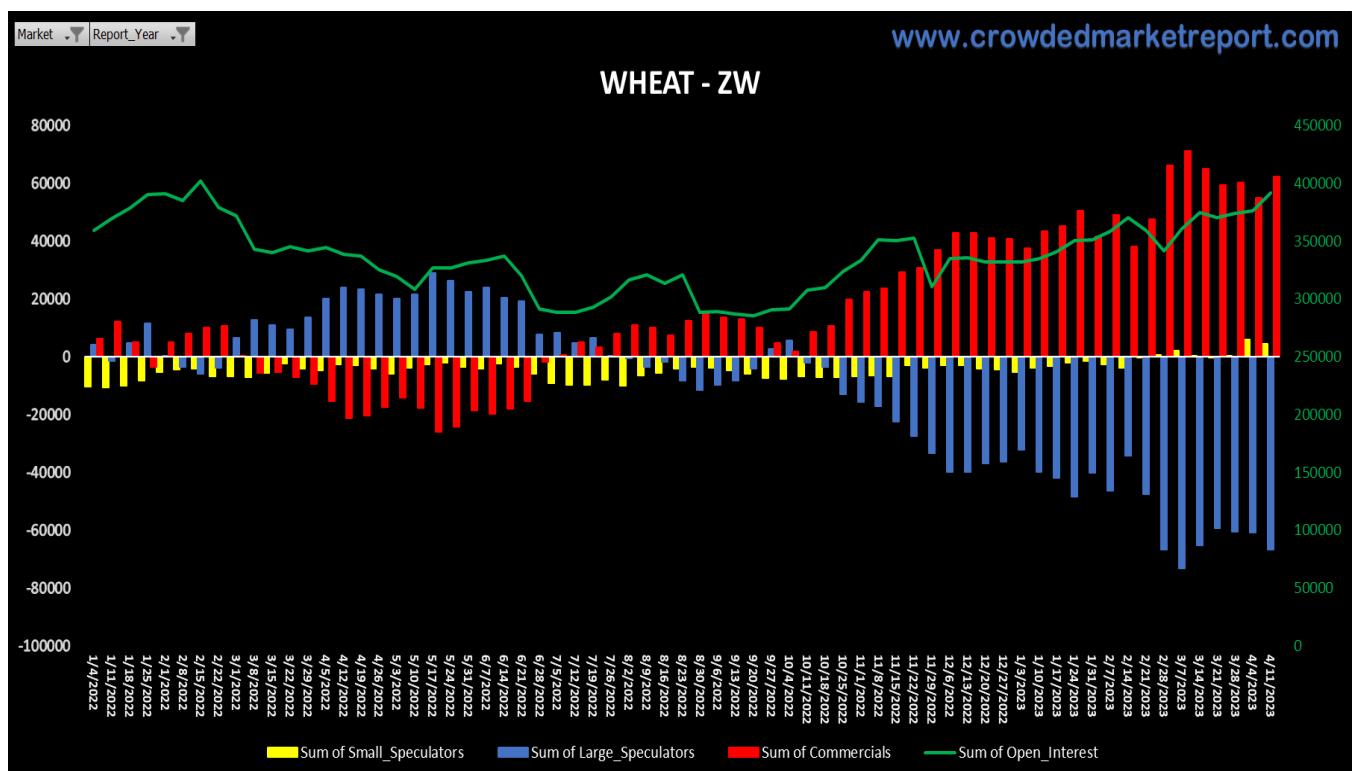
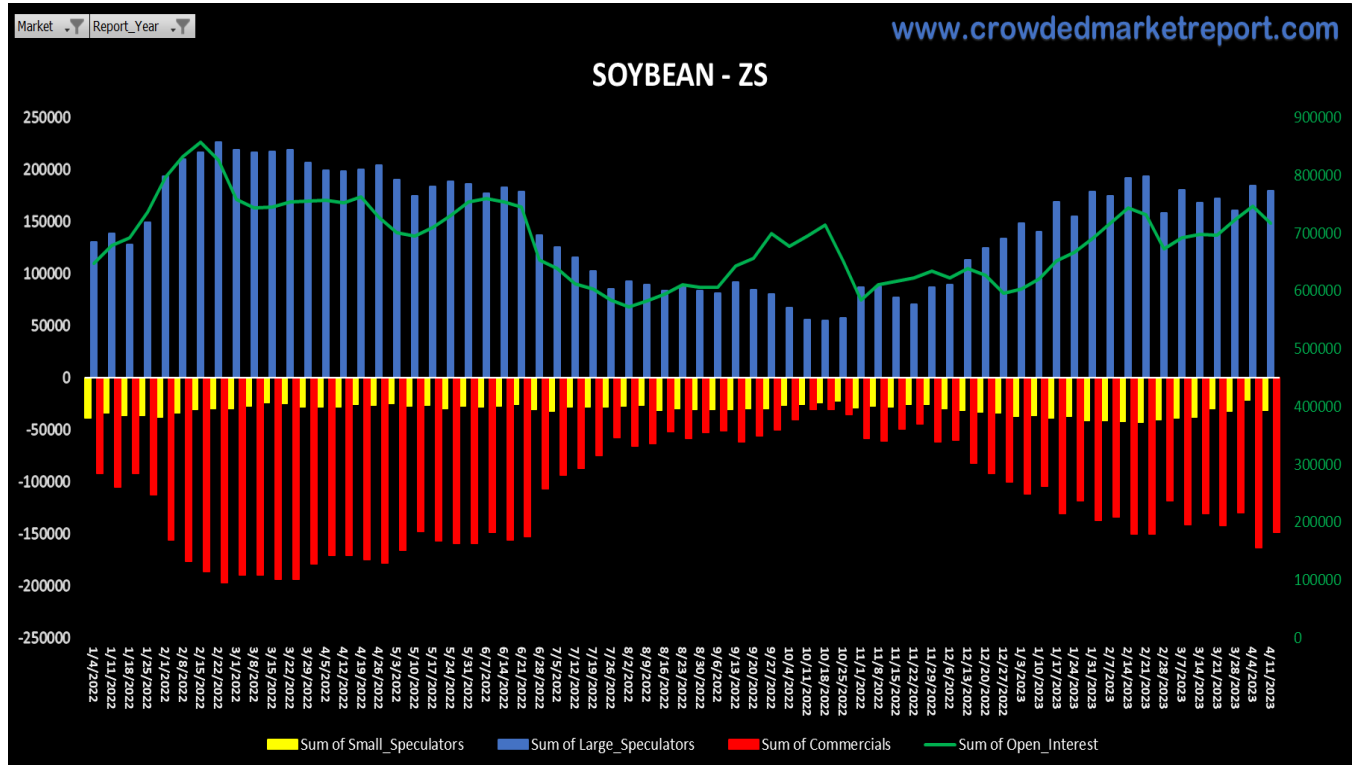


Speculators remain very short Palladium, even though it has been over a month since Palladium made lows:



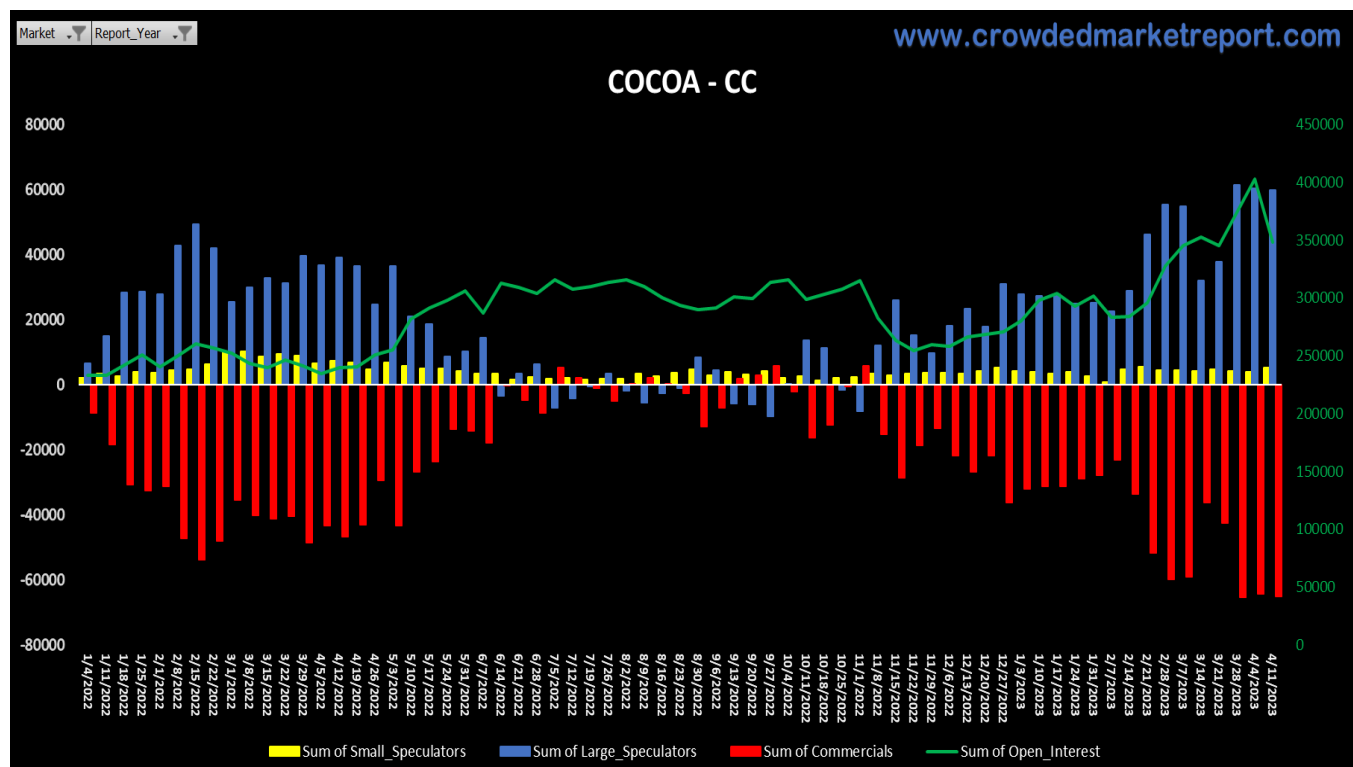
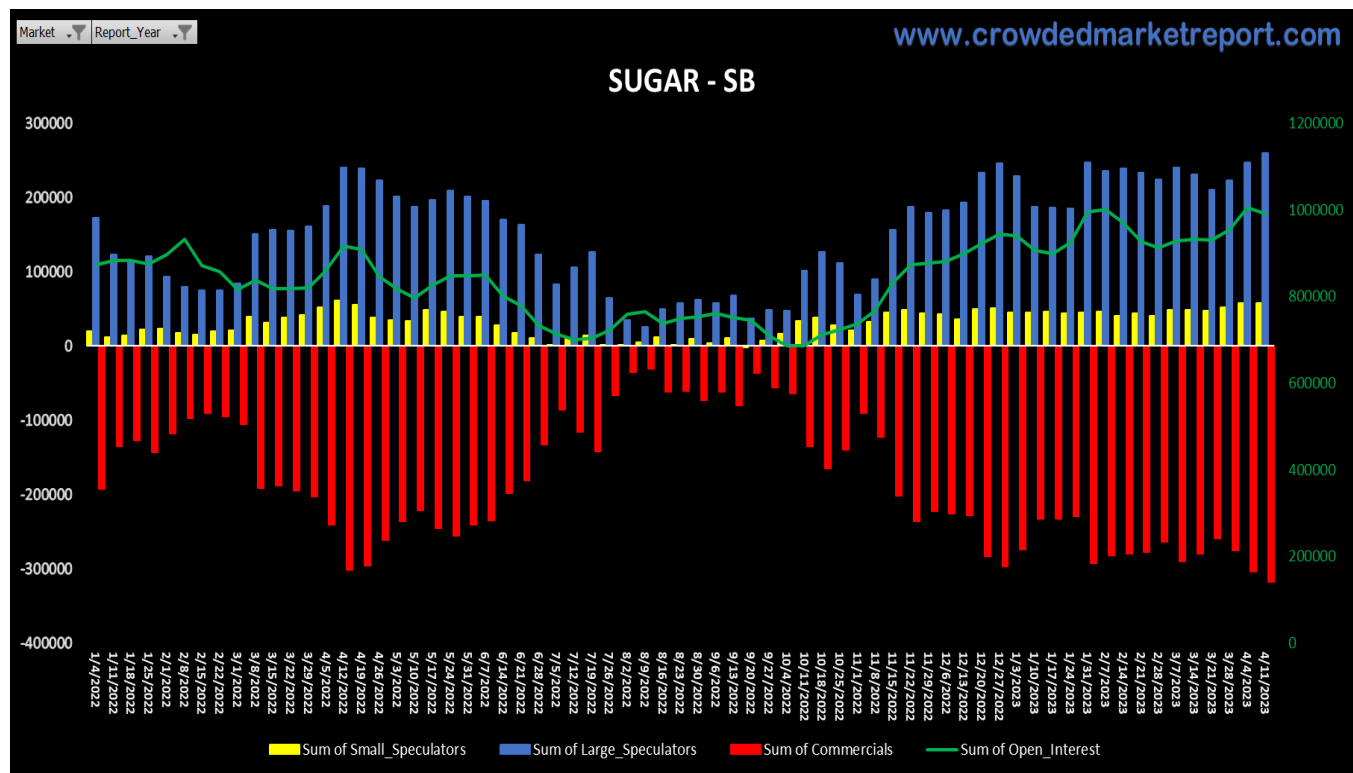
Grains

Nothing exciting in Grain positioning, although we continue to see Speculators long Soybeans and short Wheat:



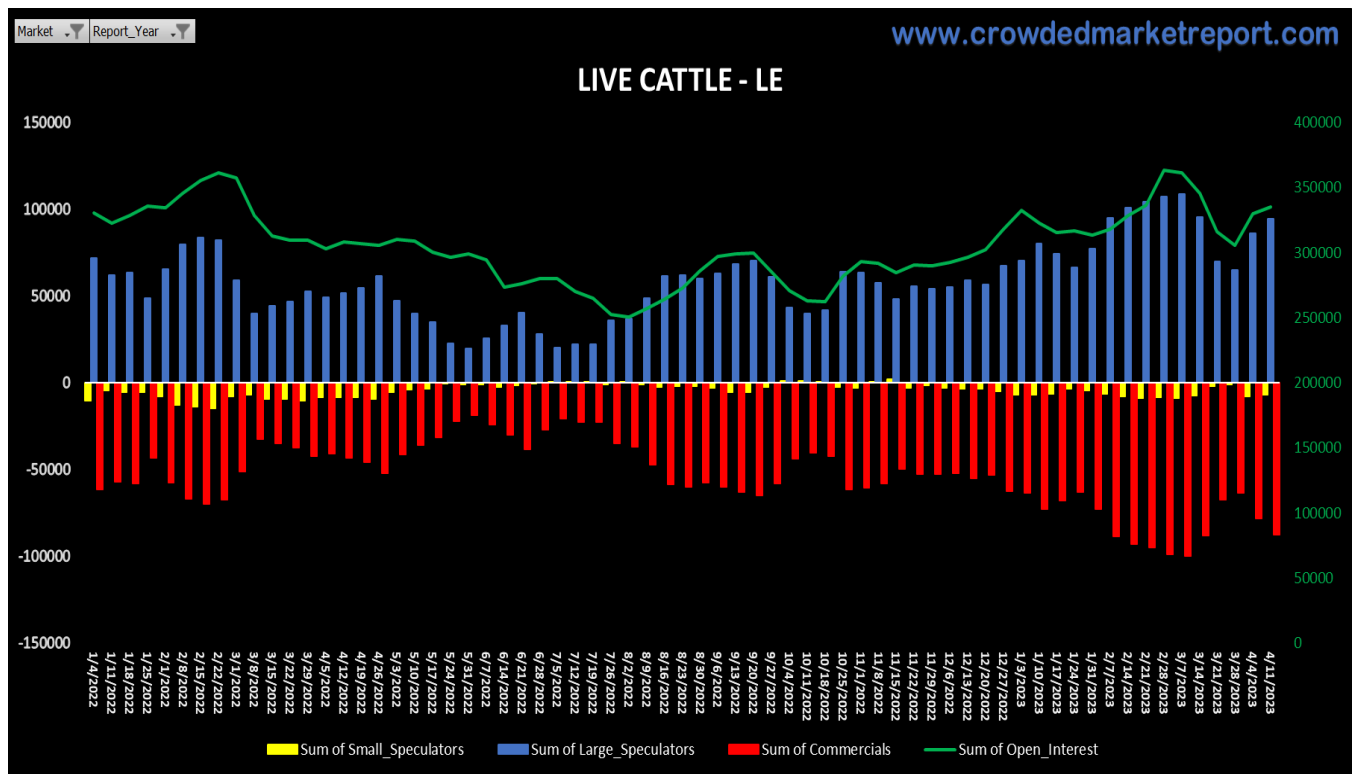
Softs

I took positions last week in two Softs markets, shorting both Sugar and Cocoa. Because of lack of liquidity in these markets, plus the difficulty in reading news failures, the trades were half sized positions in each market:

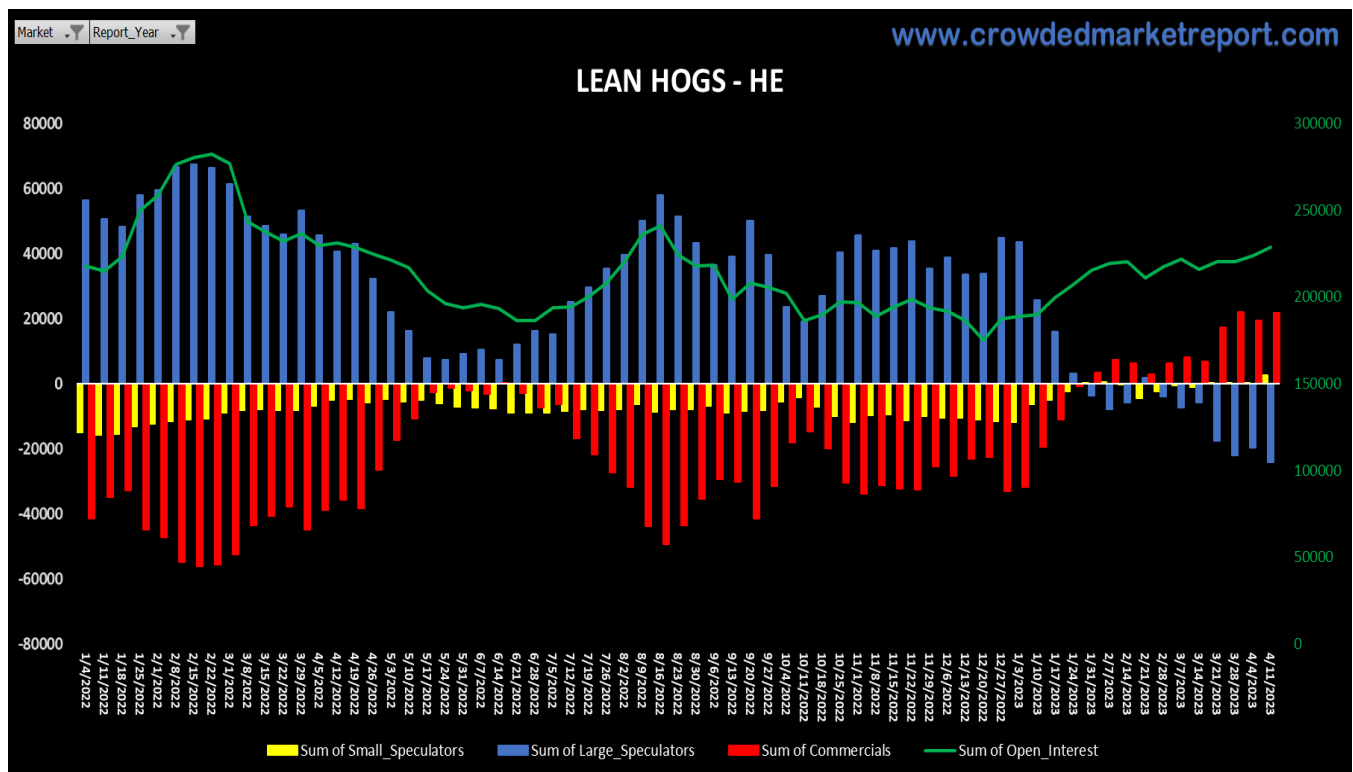


Livestock

Speculator positioning is again getting close to max long in Live Cattle:

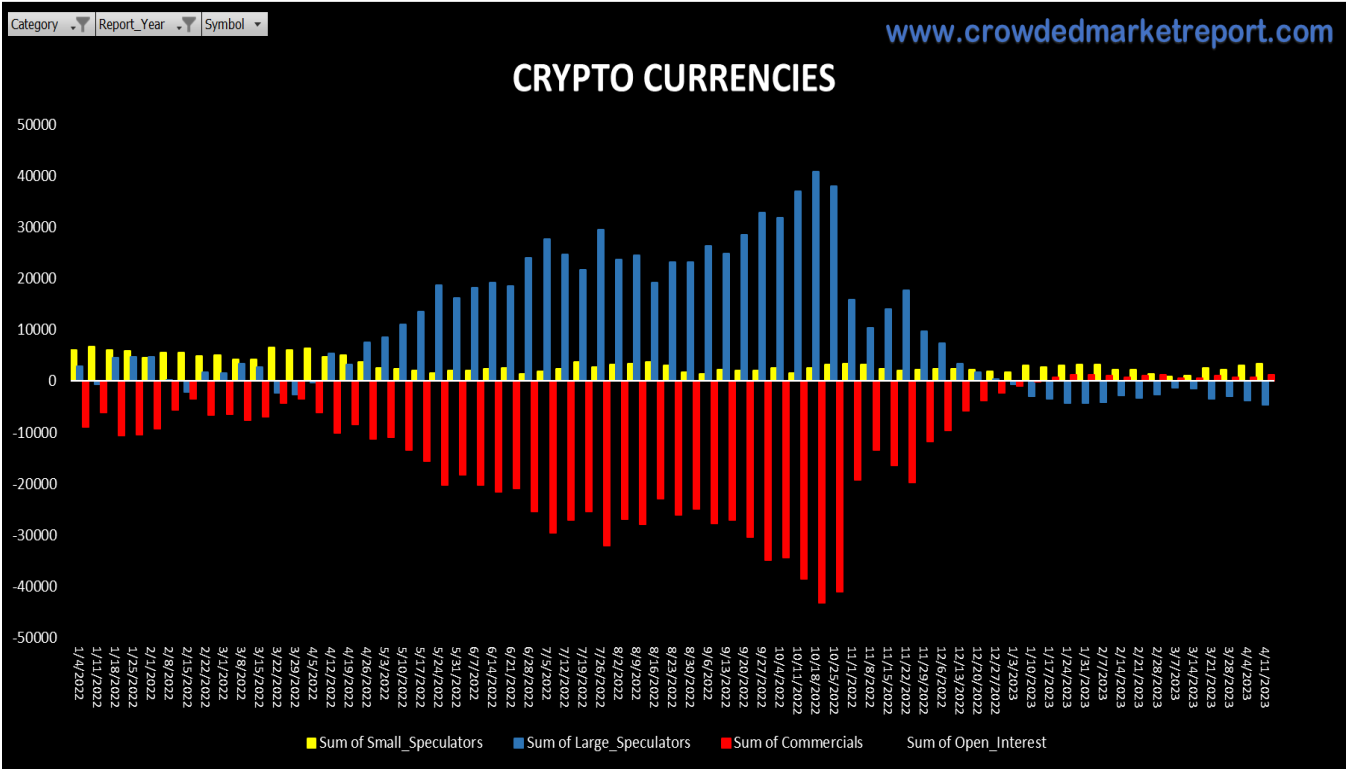


Speculators continue to get short Lean Hogs:



Crypto Currencies

Crypto continues to move higher right in the face of those who gave up after the Bankman Fried scandal:



Putting it All Together...

Positioning right now does not seem to agree with each other across asset classes. COT would indicate a move higher in both Fixed Income and Equities, but we are seeing a possibility of a stronger US Dollar as well, in particular versus British Pound and Euro, which on the surface would indicate higher US rates (lower bonds). Having said that, it is really only the US rates relative to those in Europe and the UK that should affect this, so it is possible the British and European Bond markets will just underperform US Bond markets from here. This possible move higher in the US Dollar does reconcile with the idea of being short commodities in general, in particular Gold.

As of yet, I have not seen any capitulation by equity bears at all. They are dug in and waiting for the coming recession and corresponding earnings downgrades to bail them out. I continue to believe they are in for continued disappointment with that idea and that until there is some capitulation the stocks market is going to continue higher. We did see stocks go down on Friday with the S&P down 1 point at the close and the Nasdaq down a whopping 10 points. There have been no signs in either positioning or market action that would indicate the market is turning down as of yet. It is pretty clear the market has gone up quite fast and at some point, this momentum will have to slow, but for me, looking at the continued bearish sentiment and positioning, I will stay long.

I like to do periodic analysis of my trading to make sure the process is not losing robustness. I have done some of this below as an example. For the purposes of this analysis, I have taken every trade I have mentioned on here since the start of this year and ignored any "trading around" of positions that were done due to the COT data issues earlier in the year. I just took every trade as entry, stop, and exit, based on my process using COT.

To keep things easy, I assumed a portfolio of \$1 million and used 1% risk (\$10,000) per trade to calculate the number of contracts traded. I calculated the difference between the entry price and the stop level, then backed into the position sizing. For example, if my long entry price for a contract was \$100, my stop level was \$95 and each point equals \$100, then my size would be calculated as follows: \$ risk divided by ((entry minus stop) times \$ per point $\rightarrow \$10,000 / ((\$100 - \$95) \times \$100) \rightarrow \$10,000 / \$500 \rightarrow 20$ Contracts. To further clarify, if 20 contracts went down by 5 points to my stop level, the most I would risk is \$10,000 on paper (I know slippage may occur, just trying to clarify for example purposes):

$$20 \text{ contracts} \times 5 \text{ points} \times \$100 \text{ per point} = \$10,000.$$

There has been a total of 19 trades during 2023 at the time of writing this report. Of those, 12 have been profitable and 7 were losers. This is a much higher win ratio than the 37% I expected, so that is positive. This also helps explain why the return for the first quarter of the year is much higher than expected. The total return so far for 2023 is about 27%, with the largest drawdown being around 7%. Of the 12 profitable trades, about ~60% of the profit comes from 4 trades, which is pretty typical over time and helps to stress the importance staying disciplined through winning trades since over time, it is those small number of trades that will make the bulk of the profit. Unfortunately, it is impossible to know beforehand which trades will end up being this important Profit & Loss driver, so just sitting on the winners until they play out whether that be a couple of weeks, or a few months is extremely important over time.

This has certainly been an unusually good run for my process, and it gets me wondering if there is a mean reversion about to happen. My understanding of statistics tells me that this does not necessarily have to be the case, and regardless of what has happened in the recent past going forward over time, there should still be a 37% chance of my process producing winning trades based on long-term historical performance. For example, if I flip a coin and get heads 5 times in a row, which does not mean the next coin flip result will have a higher chance of heads, it will still be 50%. The trades should have a payoff of ~4.5 to 1 versus losing trades based on long-term historical performance. So far so good, I shall remain disciplined.

Please note this analysis was done based on continuous contract pricing for each market and may not match up with actual trades completed on the actual futures contract. Analysis may include unintentional human error.

Market	Futures Contract Symbol	Long/Short	Entry Date	Entry Price	Stop	Contracts per Trade	Exit Date	Exit Price	Loss/Win	\$ Per Point	\$ Risk	\$ Reward	Reward/Risk
Cotton	CT	Long	10/31/2022	\$ 72.00	\$ 70.20	11	4/14/2023	\$ 82.93	Win	\$ 500	\$ 9,900	\$ 60,115	6.1
2-year notes	ZT	Long	11/4/2022	\$ 101.56	\$ 101.28	18	1/19/2023	\$ 103.00	Win	\$ 2,000	\$ 10,125	\$ 51,750	5.1
Silver	QI	short	12/21/2022	\$ 24.20	\$ 24.52	6	1/11/2023	\$ 23.48	Win	\$ 5,000	\$ (9,600)	\$ 21,600	2.2
Lumber	LBS	Long	12/20/2022	\$ 368.00	\$ 362.00	15	1/5/2023	\$ 365.00	Loss	\$ 110	\$ 9,900	\$ (4,950)	-0.5
30-year bonds	ZB	Long	1/5/2023	\$ 127.53	\$ 126.47	9	1/19/2023	\$ 131.75	Win	\$ 1,000	\$ 9,563	\$ 37,969	4.0
Gasoline	RB	Short	1/27/2023	\$ 259.35	\$ 271.35	2	3/3/2023	\$ 275.04	Loss	\$ 420	\$ (10,080)	\$ (13,180)	-1.3
10-Year Notes	ZN	Long	1/24/2023	\$ 115.03	\$ 114.22	12	1/27/2023	\$ 114.61	Loss	\$ 1,000	\$ 9,750	\$ (5,063)	-0.5
Gold	GC	Short	2/2/2023	\$ 1,930.80	\$ 1,975.20	2	2/16/2023	\$ 1,851.80	Win	\$ 100	\$ (8,880)	\$ 15,800	1.8
Nasdaq	NQ	Long	1/20/2023	\$ 11,677.00	\$ 11,308.00	1	3/8/2023	\$ 12,228.00	Win	\$ 20	\$ 7,380	\$ 11,020	1.5
Yen	6J	short	2/10/2023	\$ 76.34	\$ 77.34	8	3/9/2023	\$ 73.50	Win	\$ 1,250	\$ (10,000)	\$ 28,400	2.8
2-year notes	ZT	Long	2/16/2023	\$ 102.00	\$ 101.44	9	2/21/2023	\$ 101.80	Loss	\$ 2,000	\$ 10,125	\$ (3,516)	-0.3
10-year notes	ZN	Long	3/3/2023	\$ 111.09	\$ 110.19	11	3/24/2023	\$ 116.11	Win	\$ 1,000	\$ 9,969	\$ 55,172	5.5
Soybean Meal	ZM	Short	3/8/2023	\$ 485.70	\$ 498.00	8	3/22/2023	\$ 451.60	Win	\$ 100	\$ (9,840)	\$ 27,280	2.8
Russell	RTY	Short	3/16/2023	\$ 1,786.00	\$ 1,722.00	2	3/22/2023	\$ 1,741.00	Win	\$ 100	\$ 12,800	\$ 9,000	0.7
Soybean Oil	ZL	Long	3/15/2023	\$ 56.34	\$ 54.99	12	3/22/2023	\$ 54.64	Loss	\$ 600	\$ 9,720	\$ (12,240)	-1.3
Nasdaq	NQ	Long	3/14/2023	\$ 12,337.00	\$ 11,806.00	1	3/24/2023	\$ 12,890.00	Win	\$ 20	\$ 10,620	\$ 11,060	1.0
Dow	YM	Long	3/24/2023	\$ 32,434.00	\$ 31,657.00	1	4/14/2023	\$ 34,037.00	Win	\$ 10	\$ 7,770	\$ 16,030	2.1
Gold	GC	Short	3/24/2023	\$ 1,983.80	\$ 2,006.50	4	4/4/2023	\$ 2,038.00	Loss	\$ 100	\$ (9,080)	\$ (21,680)	-2.4
Gold	GC	Short	4/6/2023	\$ 2,035.60	\$ 2,049.20	7	4/13/2023	\$ 2,055.00	Loss	\$ 100	\$ (9,520)	\$ (13,580)	-1.4

Current Positions

- Long Cotton from 4/6/2023. Stop on close below the 10/31/2023 low.
- Short Sugar from 4/12/2023, stop on a close above the 4/12/2023 high.
- Short Cocoa on 4/14/2023, stop on close above the 4/14/2023 high.
- Long S&P from 4/14/2023, stop on close below 4/10/2023 low.

Last Week's Trades

- Stopped on Gold short on April 13 close.
- Shorted Sugar on April 12 close, stop on a close above the April 12 high.
- Shorted Cocoa on April 14 close, stop on close above the April 14th high.
- Sold Long Dow on Friday's close. This trade was risking 489 points on entry and ended up making 1,667 points for a return to risk ratio of about 3.4 times. This is about typical for winning trades in CMR process.
- Bought S&P on Fridays close, with a stop on a close below the April 10 Low.

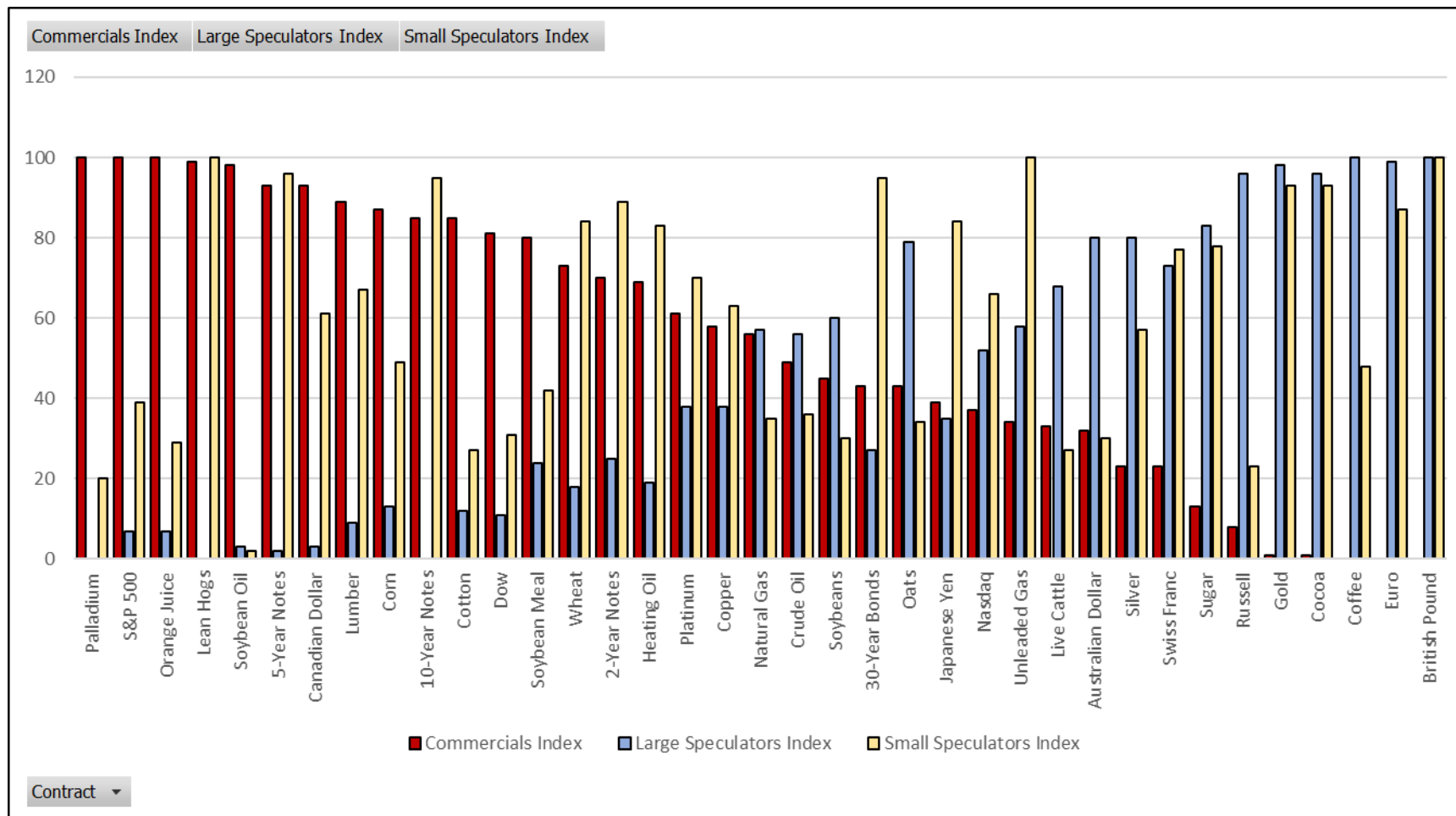
Appendix

Week over Week Heat Map

Contract	Sector	Comm Variance	LG Spec Variance	SM Spec Variance	4/16/2023			4/9/2023		
					Commercials	Large Specs	Small Specs	Commercials	Large Specs	Small Specs
30-Year Bonds	Fixed Income	-22	-1	7	43	27	95	65	28	88
10-Year Notes	Fixed Income	-3	-4	1	85	0	95	88	4	94
5-Year Notes	Fixed Income	-5	2	16	93	2	96	98	0	80
2-Year Notes	Fixed Income	4	-3	-7	70	25	89	66	28	96
Nasdaq	Equities	-3	28	-34	37	52	66	40	24	100
SP 500	Equities	40	7	-61	100	7	39	60	0	100
Dow	Equities	-19	11	31	81	11	31	100	0	0
Russell	Equities	-16	14	-7	8	96	23	24	82	30
Live Cattle	Livestock	-47	40	-33	33	68	27	80	28	60
Lean Hogs	Livestock	1	-5	6	99	0	100	98	5	94
Cocoa	Softs	1	-4	28	1	96	93	0	100	65
Sugar	Softs	7	-9	-22	13	83	78	6	92	100
Orange Juice	Softs	0	7	-31	100	7	29	100	0	60
Coffee	Softs	-20	16	38	0	100	48	20	84	10
Cotton	Softs	-9	2	19	85	12	27	94	10	8
Lumber	Softs	5	-3	13	89	9	67	84	12	54
Gold	Metals	1	-2	3	1	98	93	0	100	90
Silver	Metals	-7	2	35	23	80	57	30	78	22
Palladium	Metals	4	-5	-4	100	0	20	96	5	24
Platinum	Metals	13	-14	32	61	38	70	48	52	38
Copper	Metals	-7	14	-7	58	38	63	65	24	70
Australian Dollar	Currencies	10	-8	-2	32	80	30	22	88	32
British Pound	Currencies	-4	12	0	0	100	100	4	88	100
Canadian Dollar	Currencies	-1	3	21	93	3	61	94	0	40
Japanese Yen	Currencies	7	-33	4	39	35	84	32	68	80
Euro	Currencies	-6	10	17	0	99	87	6	89	70
Swiss Franc	Currencies	-6	13	-1	23	73	77	29	60	78
Crude Oil	Energies	-29	20	20	49	56	36	78	36	16
Unleaded Gas	Energies	-16	10	28	34	58	100	50	48	72
Heating Oil	Energies	-28	15	23	69	19	83	97	4	60
Natural Gas	Energies	7	-8	1	56	57	35	49	65	34
Corn	Grains and Seed Oils	-1	-1	-5	87	13	49	88	14	54
Oats	Grains and Seed Oils	31	-15	-46	43	79	34	12	94	80
Wheat	Grains and Seed Oils	13	-12	-16	73	18	84	60	30	100
Soybeans	Grains and Seed Oils	5	-4	-6	45	60	30	40	64	36
Soybean Meal	Grains and Seed Oils	-4	2	12	80	24	42	84	22	30
Soybean Oil	Grains and Seed Oils	-2	3	2	98	3	2	100	0	0

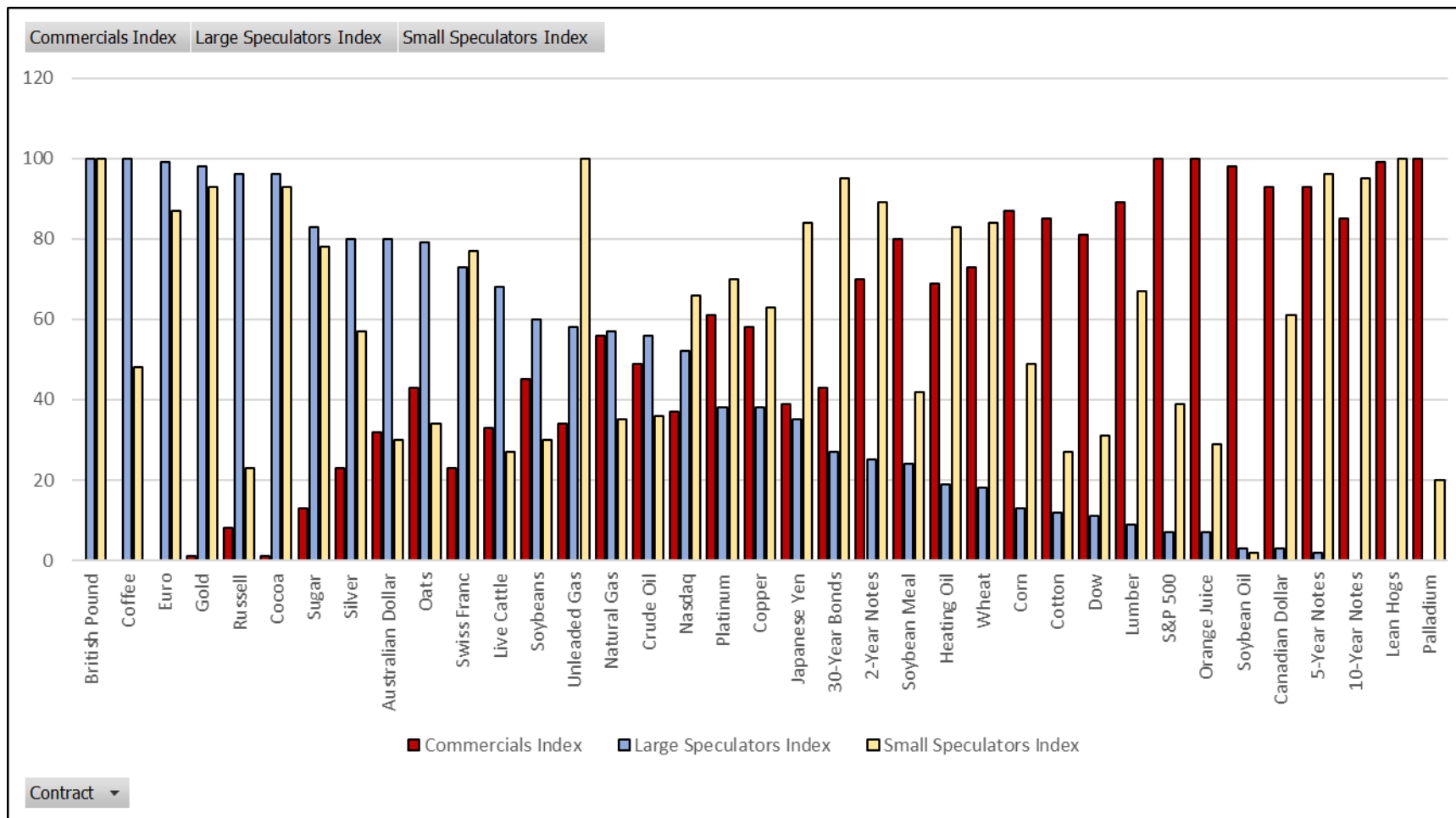
Overall Market – Sorted by Commercials

The chart displays where Commercials are positioned longest to shortest.



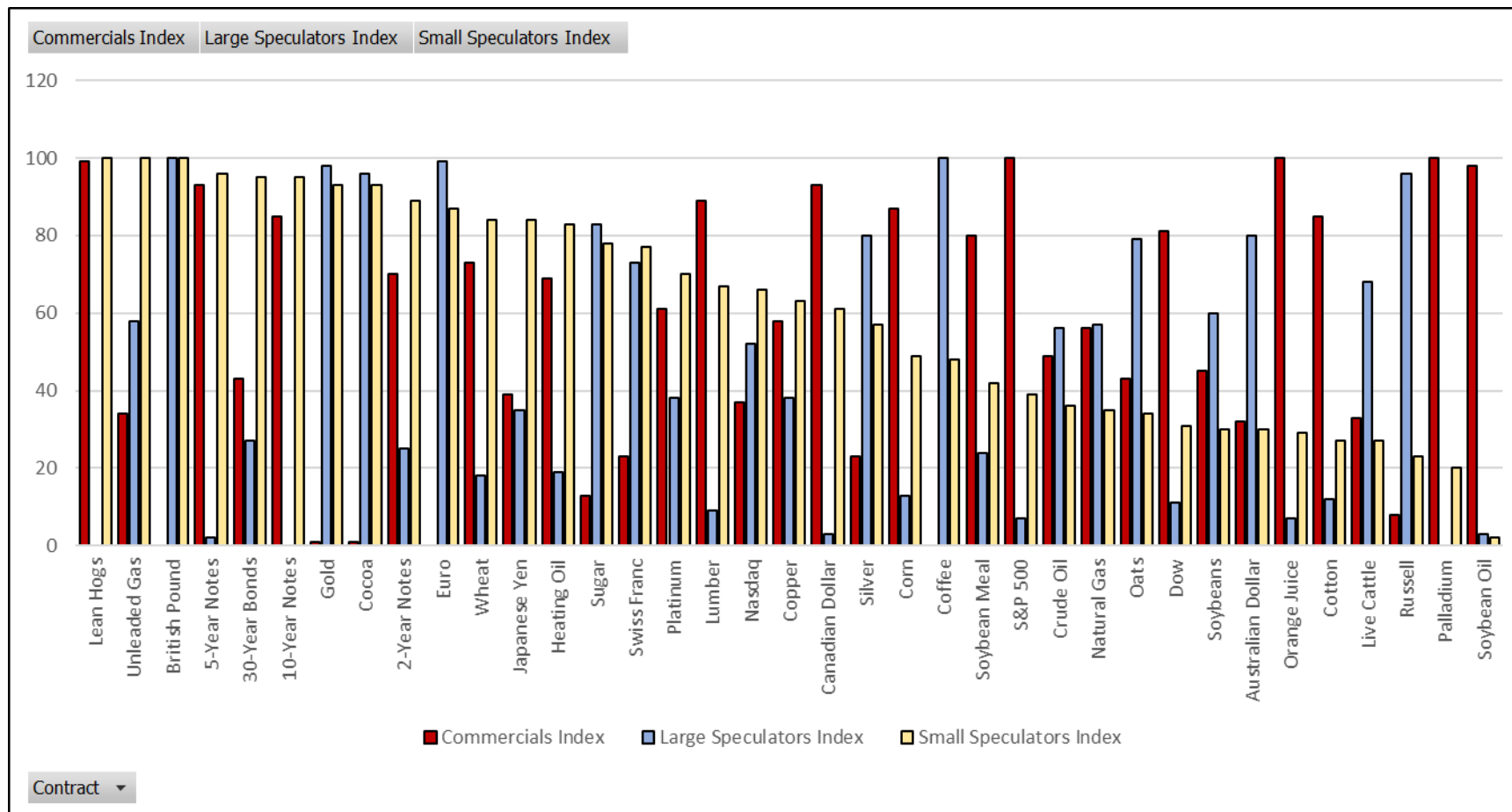
Overall Market – Sorted by Large Speculator

The chart displays where Large Speculator are positioned longest to shortest.



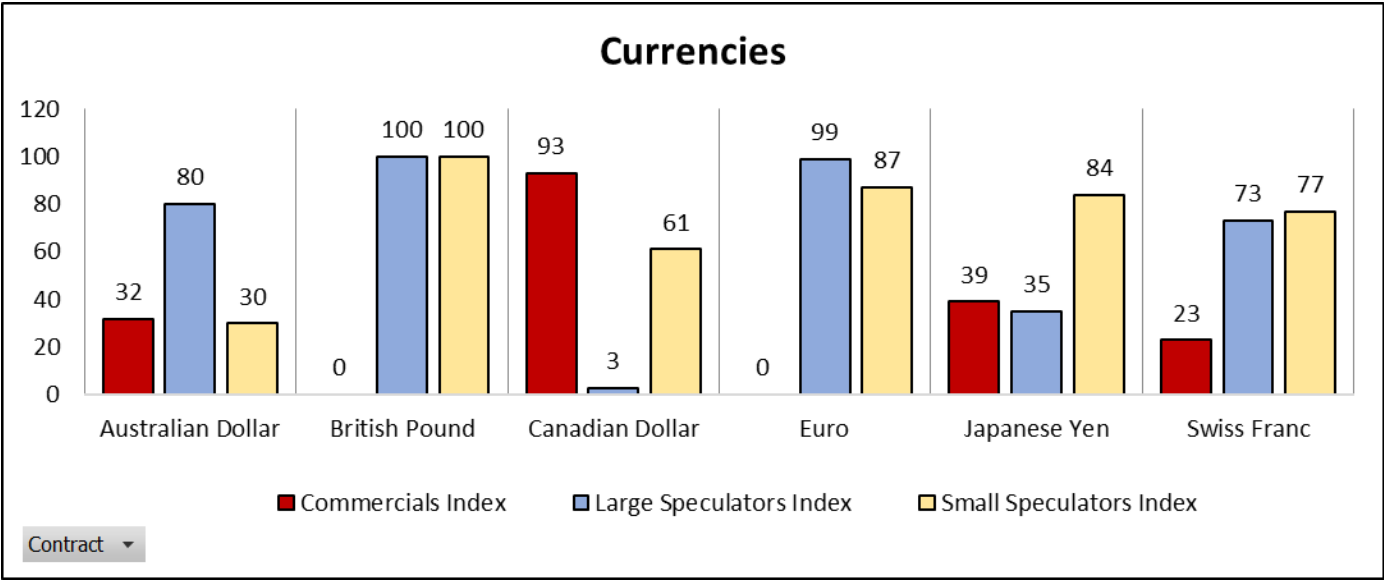
Overall Market – Sorted by Small Speculator

The chart displays where Small Speculator are positioned longest to shortest.

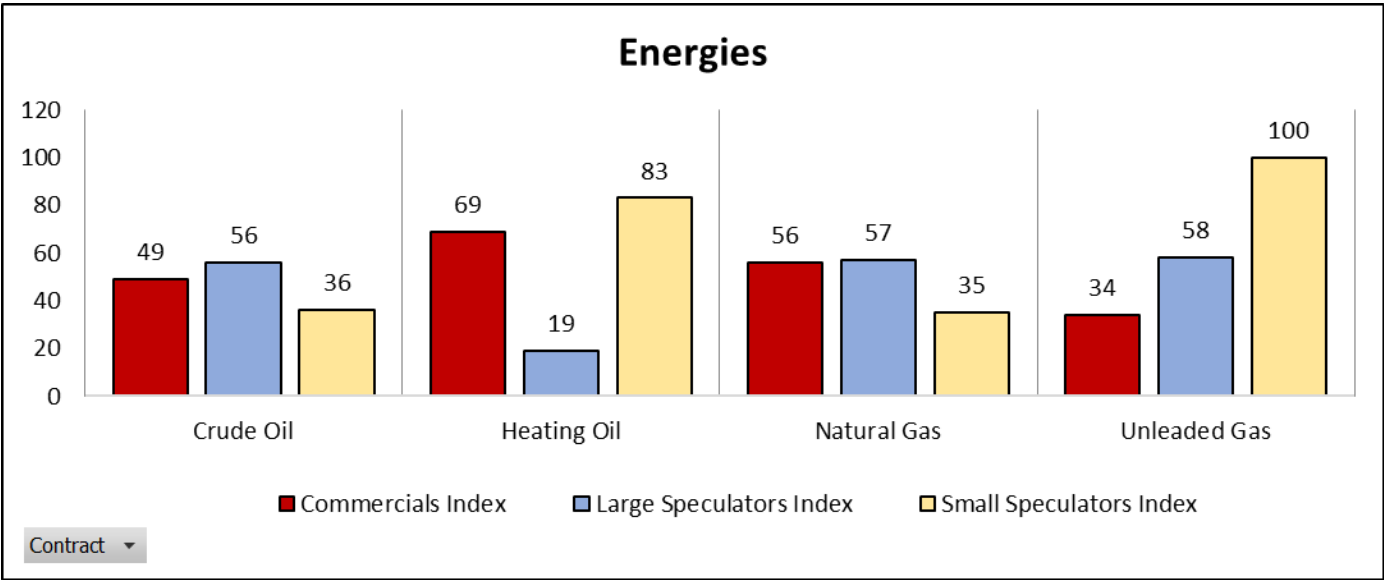


Sectors

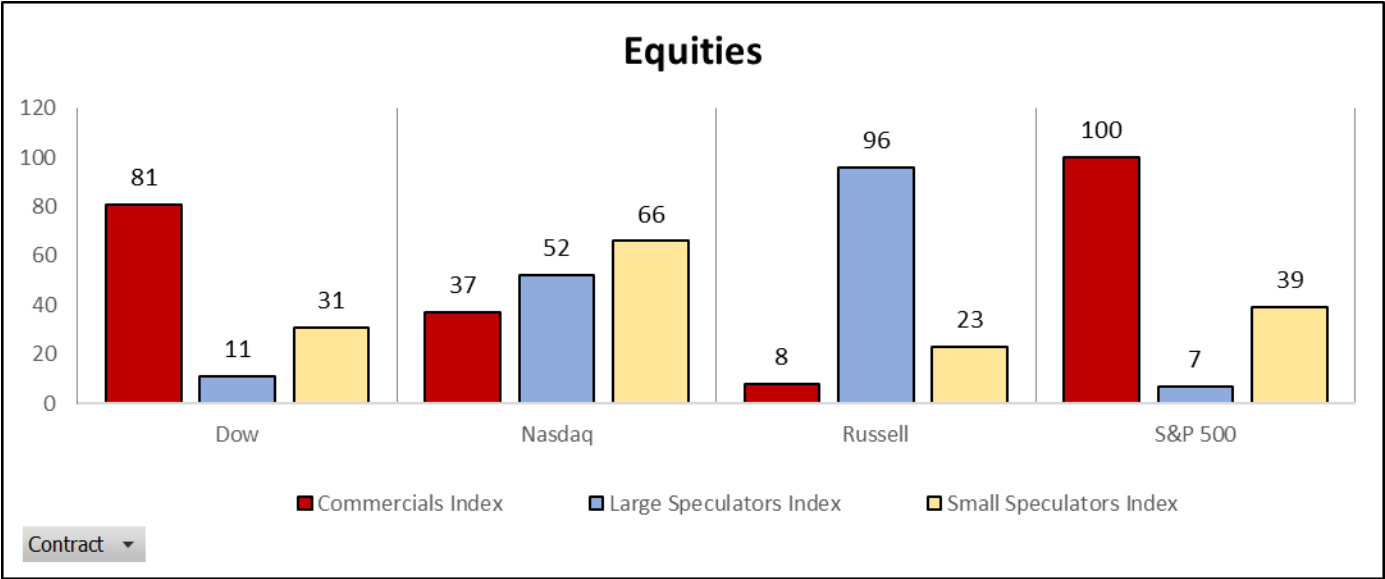
Currencies



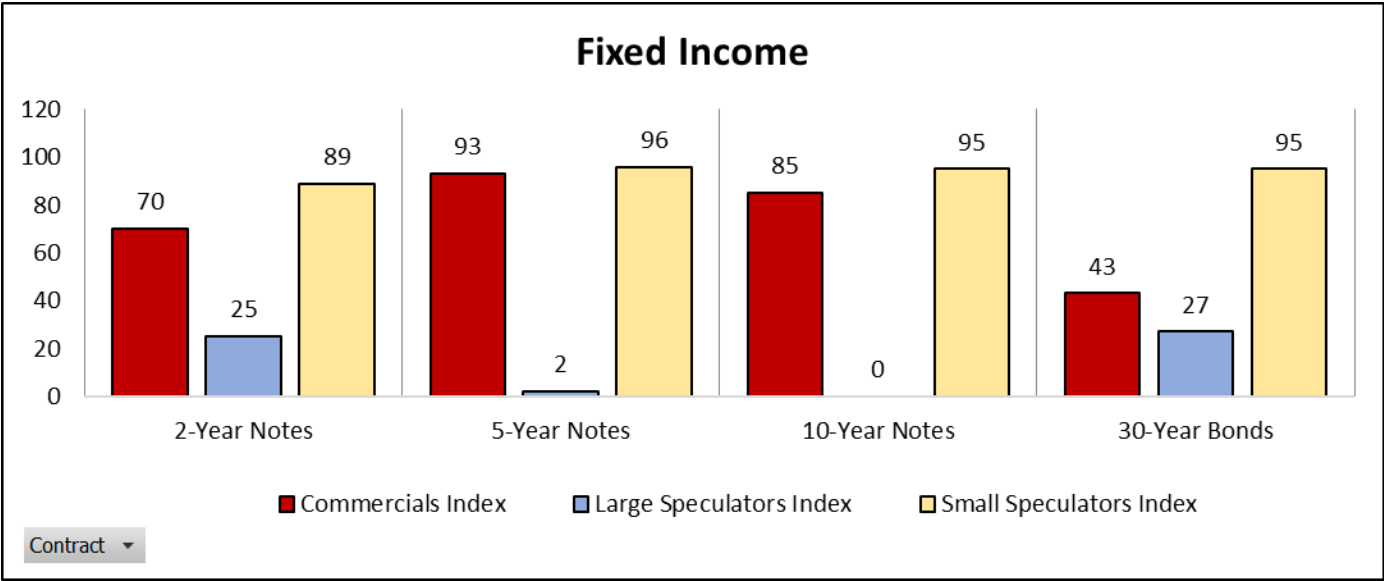
Energies



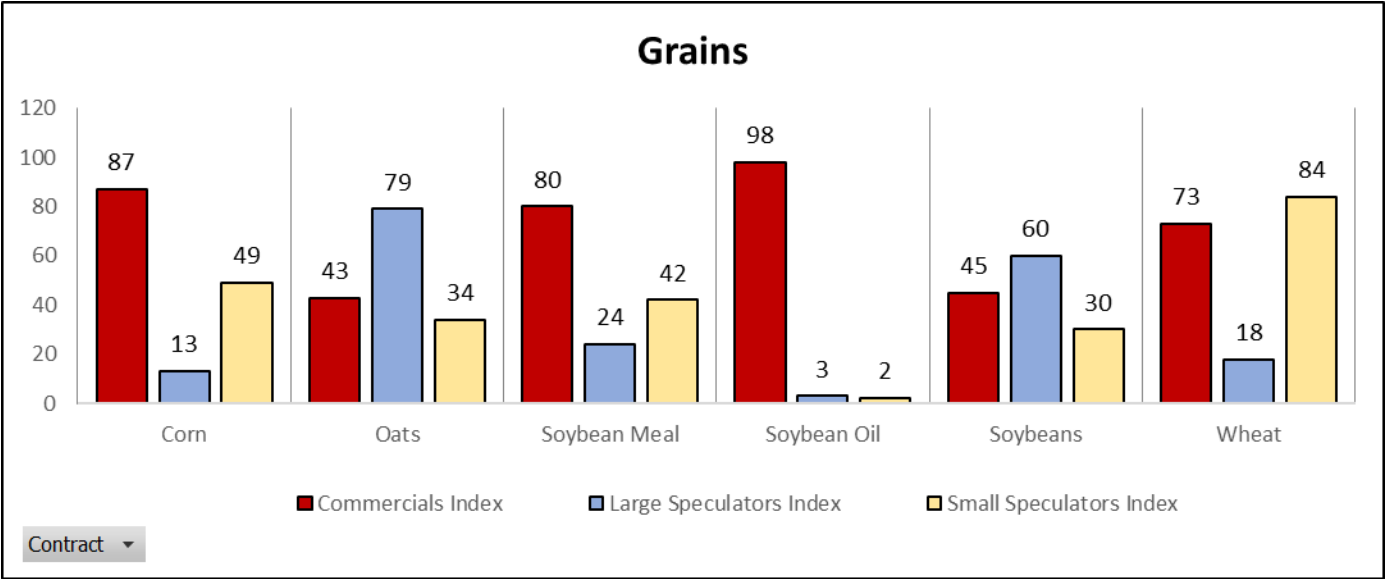
Equities



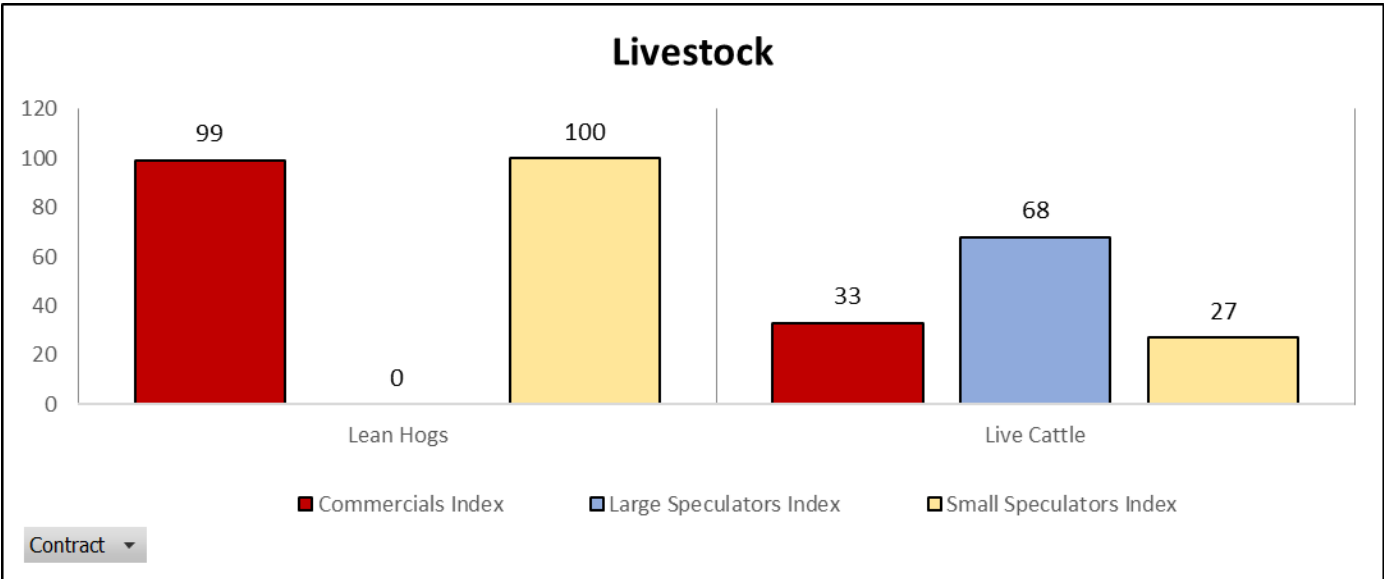
Fixed Income



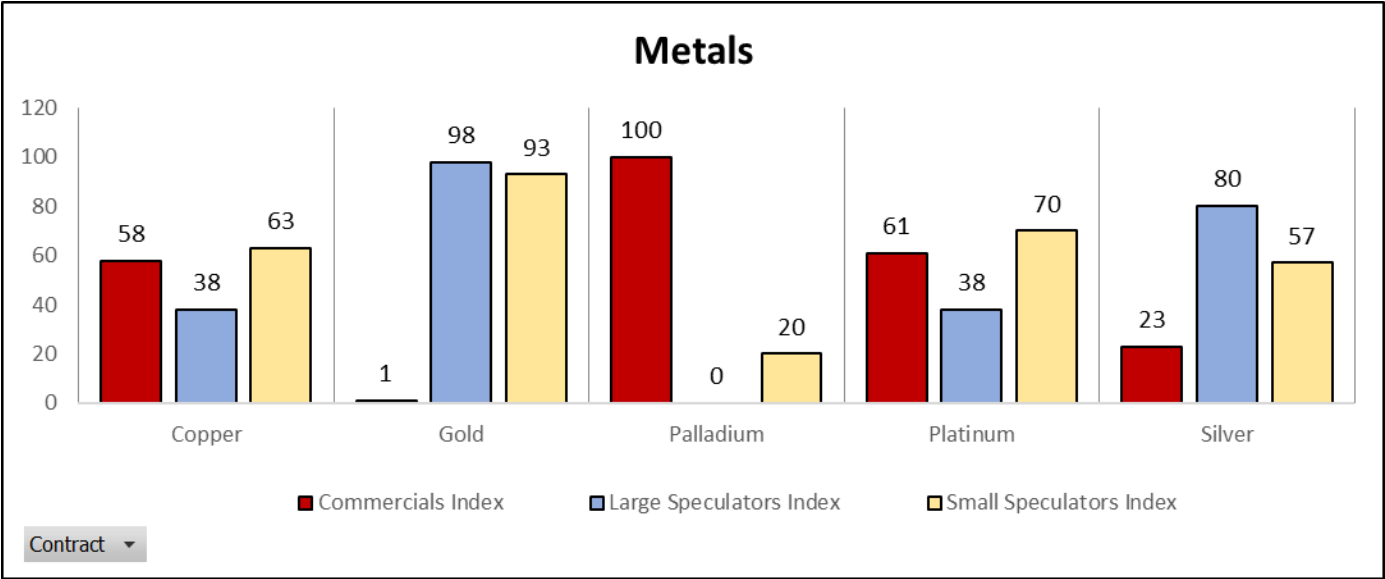
Grains



Livestock



Metals



Softs

