QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 7, 2008 Issue 14

Market Overview

Summary of Recent Active Studies (see http://QuantifiableEdges.blogspot.com for details)

Study Date	Description	Time span	Bias
March 5, 2008	Reversal Bars	1-10 Days	Bullish
March 5, 2008	CBI of 8	1-15 days	Bullish
February 27, 2008	Significance of Lagging Nasdaq	1-10 weeks	Bearish
February 12, 2008	Contraction of range	20 days	Bullish
February 1, 2008	FTD short-term implications	long-term	Bearish

Intermediate-term Outlook (2 weeks – 2 months) – neutral – updated 2/28/2008

At the end of January the market hit levels of "oversold" by several different measures. Many of the more significant readings came from breadth measures such as the massive number of 52-week lows, the McClellan Oscillator and the Quantifiable Edges CBI. Nearly everything I looked at told me the market had endured enough selling and that it was bound to rally for a while. Readings suggested a multi-week rally at a minimum and a possibility of an intermediate-term bottom.

A retest of the lows also seemed to be a fairly strong possibility. That retest has yet to arrive. We are now 5 weeks from the January bottom. The S&P 500 is 8.7% off its January lows, but really hasn't made any headway in the last 3 ½ weeks. Most of the bullish studies I referenced back then are no longer exerting much influence. In their place is a batch of new studies – most of which have a bearish tilt.

The newest of these studies, "The Intermediate Term Significance Of A Lagging Nasdaq" was posted this morning. It suggested that with the NYSE composite hitting new 5-week highs, the degree with which the Nasdaq is currently lagging the NYSE has historically been bearish. Combined with other intermediate-term studies such as the Triangles and FTD Short-term Implications the picture my research is painting is becoming less rosy.

It's fairly easy to discount or make excuses for results we don't like. Take this morning's lagging Nasdaq study, for instance. Many of the big name Nasdaq stocks like Apple, Google, Baidu and Research In Motion were leaders throughout 2007. Bear markets frequently force changes in leadership. Therefore, I wouldn't expect the above stocks to lead now as they did last year. But just because I can come up with reasons an indicator or study may not be relevant this time, doesn't mean it isn't. Studies should be considered with an open mind and not easily dismissed. When several of them begin to point in one direction, perhaps it's time to listen.

I'm reticent to turn outright bearish at this point since the readings near the January lows did have such a bullish tilt. Also the market has started to put in a series of higher lows which is allowing bases to build and providing support for the indices. For the time being, therefore I am going to let the short-term analysis act as the guide and move the intermediate-term outlook to neutral.

Short-term Outlook (1-10 days) – positive – updated 3/7/08

The S&P 500 made a new closing low today after selling off 2.2%. Down volume made up nearly 95% of all volume on the NYSE. Total volume actually declined from yesterday's levels and was also below the 50-day average. This was the 2nd day in the last 5 that downside volume made up more than 90% of total volume. While interesting, this doesn't mean much on its own. Performance in periods following two 90% down volume days in a week has been very mixed. It has also led to some very high volatility – including the crash of '87 (bad) and the August bottom of '98 (good).

The CBOE put/call ratios gave some interesting readings today as well. The equity-only put/call ratio, which has been tracked since October of 2003, posted a reading of 1.12 on Thursday. There have only been two other days with reading this high – June 14, 2004 and August 6, 2004. The June reading led to a brief bounce that lasted 7 days before the market started its next leg lower. The August reading led to a two day bounce. The low was taken out 3 days later by a whisker. That then marked the intermediate-term low as the market went on to stage a nice rally from there.

The CBOE total put/call ratio came in at 1.27. While high, this isn't nearly as extreme as the equity p/c discussed above. What is interesting here is that this marks the 7th day in a row where the total put/call ratio has closed at 1.10 or above. Going back to 1995 the only other time this has happened was August 3, 2007. That led to a 3-day rally before the final leg down of that selloff began.

The employment report will come out in the morning and should serve to set the stage for what's to come. I looked back at the performance of the SPY on the day of a employment report when the market had dropped at least 1% the day before. Performance was generally in line with other days following a 1% drop. Of the 21 occurrences, 10 were winners and 11 losers. The average win was larger than the average loss, so buying was overall net profitable. When looking at *all* days following a 1% drop, 56% of them led to gains the next day and the average win was slightly larger than the average loss.

I also looked at all instances where the SPY was trading below its 200ma and gapped on the morning of an employment data release. Fourteen times the SPY gapped up more than 0.5% on the morning of an employment report. One time it closed at its open, four times it finished lower than its open and nine times it finished above its opening price. In total another 8% was gained from open to close in these 14 instances. When the SPY gapped down more than 0.5% on the morning of an employment report the results were negative. Of the nine occurrences, one broke even, two made gains, and the other six were losers over the course of the day. This could be a function of a small sample set since large gaps lower in downtrends overall have had quite positive expectancy.

More relevant to our trading is the fact that the CBI rose once again today from 6 to 8. It has now passed the threshold of 7 where I normally begin taking on index exposure. I included a SPY trade in the section below, but I would suggest very small size. I'm wary because although individual stocks are extended, the index itself isn't. The SPY is just now starting to break down out of its recent range. It lies about 2.5% above the intraday January lows and there's a chance of cascading action from here. Spikes to 7 or higher are more typically accompanied by a mature selloff – not a fresh breakdown, hence the reason for my caution. A reading of ten could easily occur as early as tomorrow. If it does I will then likely begin to scale into the index trades with higher allocation.

Put/call ratios along with breadth and the CBI gave extreme readings today. Still there were other measures such as total volume and the VIX that made the selling seem lackluster. With the market in "breakdown" position and not yet extended, taking it slow seems like the most prudent approach. There is already a fair amount of exposure just with the Catapult and Big 50 trades. Remember, while over 90% of all Catapult *clusters* have been profitable, the formation is back-end loaded. The early trades end up the losers and the later ones typically more than make up for it. Therefore it is important not to get overextended during the early phases of a CBI spike. The more capital you have left to allocate when things really get interesting, the better you may be able to take advantage of it. I'm not sure that we're at the later stages yet, so I'm allocating conservatively but consistently at this point.

Catapult and Capitulative Breadth Statistics

(Catapult Presentation Part 1) *(Catapult Presentation Part 2)*

Open Catapult Trades

Symbol	Trigger Date	Entry Price	Current Price	% Gain/Loss	Action
SLE	2/19/2008	$13.10	$12.73	-2.8%	bought @ $13.10
SLE	2/20/2008	$13.11	$12.73	-2.9%	bought @ $13.11
SLE	2/21/2008	$13.02	$12.73	-2.2%	bought @ $13.02
MRK	3/4/2008	$43.76	$42.39	-3.1%	bought @ $43.76
NYX	3/4/2008	$63.09	$61.60	-2.4%	bought @ $63.09
MRK	3/5/2008	$43.25	$42.39	-2.0%	bought @ $43.25
MRK	3/6/2008		$42.39		buy @ $42.39 limit
WB	3/6/2008		$27.41		buy @ $27.41 limit

Looking for a 3rd and final entry into MRK and 1st entry into Wachovia (WB).

Open Big 50 Trades

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
GRMN	3/3/2007	$58.60	$56.03	-4.4%		
GRMN	3/4/2008	$56.83	$56.03	-1.4%		
AMZN	3/4/2008	$61.67	$62.74	1.7%		sold 1/2 @ $66.00
MOT	3/4/2008	$9.70	$9.94	2.5%		

Open Catapult for ETF's Trades

none

Broad Market Large Cap CBI – 8 (3 SLE, 3 MRK, NYX, WB)

The CBI is now at 8/4. This in itself would normally be enough for me to start scaling long. As noted above, the position of the indices has me a bit hesitant to get aggressive yet.

Sector CBI Breakdown (% of stocks with active catapult triggers within each sector.)

Index	ETF	CBI %		Index	ETF	CBI %
DJ US Broker Dealers	IAI	6.90		DJ US Energy	IYE	0.00
DJ US Insurance Index	IAK	5.41		DJ US Financial	IYF	3.08
DJ US Regional Banks	IAT	2.50		DJ US Financial Services	IYG	3.50
DJ US Utilities	IDU	4.05		DJ US Healthcare	IYH	4.93
DJ US Oil&Gas Expl & Prod	IEO	0.00		DJ US Industrial Sector	IYJ	0.77
DJ US Oil Equip & Svcs	IEZ	0.00		DJ US Consumer Goods	IYK	2.72
DJ US Pharmaceuticals	IHE	5.41		DJ US Basic Materials	IYM	0.00
DJ US Healthcare Providers	IHF	2.04		DJ US Real Estate	IYR	1.22
DJ US Medical Devices	IHI	0.00		DJ US Transportation	IYT	0.00
DJ US Aerospace & Defense	ITA	0.00		DJ US Technology Sector	IYW	3.52
DJ US Home Construction	ITB	0.00		DJ US Telecommunications	IYZ	10.53
DJ US Consumer Svcs	IYC	3.95		Nasdaq 100	QQQQ	5.00

CBI percentages continue to rise steadily. Nothing is screaming "buy" just yet, though.

Additional New Trade Ideas

Longs

SPY **–** Buy *smaller than usual allocation* @ $131 limit.

Shorts

none

Additional Trades Active Table

none

Stocks and ETF's on my Radar

Ticker ***Notes***

Notable S&P 500 stocks outside my "tradable" radar

Oversold

MYL – I'd still prefer to see either a washout day or a reversal day before jumping in here.

Overbought

none.