

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

April 17, 2008

Issue 42

Market Overview

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

Study Date	Description	Time span	Bias
April 15, 2008	WR7 Down NR7	1-15 Days	Bullish
April 14, 2008	Sharp Selloff in Consolidation	20 days	Bearish
April 10, 2008	Relatively High Put/Call	20 days	Bullish
April 4, 2008	Trend Over Volatility (TOV)	20 days	Bullish
April 1, 2008	3 Surge Days	2-6 weeks	Bullish
February 1, 2008	FTD's Short-Term Implications	long-term	Bearish
March 24, 2008	Nasdaq Leadership Bullish	1-10 weeks	Bullish
March 19, 2008	Bottom Explosion 2	1-20 days	Bullish
March 19, 2008	3.5% Up Cluster	10-20 days	Bullish
March 17, 2008	Consumer Sentiment Stretch	1-12 months	Bullish

Short-term Outlook (1-5 days) –neutral – updated 4/17/08

The market put in a strong day today. A large gap up was followed by additional buying as the market never really looked back from the opening bell and held strong most of the day, finishing near its highs. Breadth and volume statistics were also impressive. I ran a multitude of tests tonight and results were surprisingly mixed.

For instance, I ran a test similar to the sharp drop in congestion that I looked at Sunday night. This time I looked at sharp rises when the ADX was less than 20 and the market failed to make a new 10-day high. The results for the S&P 500 were very strong and showed a high winning percentage and positive expectancy over the next 1-10 days. The same test on the Nasdaq had a firmly negative expectancy.

IBM surprised after the bell today and the futures are looking positive once again. I therefore looked at how the QQQQ and SPY reacted to gaps up on mornings following large gains. For the QQQQ, any time it rose at least 2.5% and then gapped up between 0.5% and 2.0% the next morning, it showed an average loss of -0.5% the rest of the day. There were 45 such occurrences. Gaps over 2% after a 2.5% runup were breakeven.

In the SPY I looked at gaps up following gains of 2% or more. If the gap up was between 0.25% and 0.5% then the rest of the day the market lost 0.44%. If the gap was above 0.5% the following morning the market actually tacked on another 0.24% during the day.

A third study I looked at involved looking at how the market performed after a day when it gapped up at least 1% and then closed at least another 1% higher. Once again the results for the Nasdaq were quite negative. There was frequently a retracement of the move over the next week or two. In fact, when the market was trading below the 200-day moving average then 55% of the QQQQ gaps were filled within 5 days and 74% within 10 days. In the case of the SPY the results were basically flat. Only 41% of them filled the gap within 5 days and 55% within 10 days.

The highly divergent results I'm finding on all these tests has me a bit puzzled. It seems as though the most likely course for the market will be to pull back and retrace at least part of today's move at some point in the next few days. It is not yet clear that we have a good entry point to attempt a short. My preference at this time is to let things play out a bit more. We're overbought on a very short-term basis (intraday charts.) Looking at daily charts, though, the market is still in congestion. I'd like to wait until the market is more clearly overbought before shorting. On the other hand, if the market can pull back a little bit over the next few days, then we may get a favorable long entry. I see no need to rush in just yet.

The one scenario that might look pretty good for aggressive traders from a short-term perspective tomorrow is if the market makes a small gap up. This could be shortable.

Intermediate-term Outlook (2 weeks – 2 months) – neutral – updated 4/14/2008

On Friday April 11th the market took a bit of a dive. The catalyst for the selloff was GE's poor earnings announcement. In a healthier market environment the large gap down at the open would have been viewed by market participants as a buying opportunity and the market would have spent the day clawing back from its losses rather than extending them. By the end of the day Friday, the S&P 500 had lost over 2% and the Nasdaq 100 had lost nearly 3%. This action is concerning.

In [tonight's blog](#), I looked at large selloff's in the past that occurred in non-trending markets and were not breakdowns. For this test I used ADX to define trend and a violation of a 10-day closing low to determine a possible break of support. The results were quite negative over every exit point from 1-day to 4-weeks out. This is the first study with bearish intermediate-term implications I've produced for several weeks.

As I mentioned in my last intermediate-term outlook a few days ago we are also seeing some of the more bullish studies from a few weeks back begin to age and expire. The first one occurred last Thursday. This Thursday the 17th both of the bullish studies from March 19th will fall off the list as their influence wanes.

Another concern is the action in the Nasdaq this week, and especially Friday. As I mentioned above, GE was the catalyst, and the prime culprit for their earnings miss was the disruption in the financial markets. You would expect financials to take this news poorly and sell off in sympathy. The Nasdaq, which had taken a leadership role over the NYSE Composite a few weeks ago, should have held up a bit better. GE is largely

unrelated to technology. Yet it fell even harder than the broad market – nearly 3% versus the S&P 500's 2%. This has moved the weekly relative strength of the Nasdaq below the NYSE's. As I've discussed in the past, the general market has typically struggled to advance when the Nasdaq has failed to take leadership from the NYSE.

It will be important to monitor the market's ability to hold above recent support levels. As noted, it has failed to break down in any way so far. Friday did move the S&P 500 and Nasdaq below their 50-day moving averages. While these are lines that many analysts looked at to possibly provide support, I find it neither surprising nor concerning that they were broken. Moving averages many times will provide support or resistance based on their slope. A moving average which has a nice up-slope serves a decent chance of providing at least temporary support. When a moving average is flat, many times it will act more as a pendulum than a support/resistance level. The recent move up in the market served to flatten out the 50-day moving averages. It may cross back and forth above and below it several times before the direction is fully determined and the moving average will begin to act as a support/resistance level again.

The late March lows are more significant in my eyes. These were around 1313 for the S&P 500. If the market can remain above these then the series of higher lows remains in tact and the baby rally has a chance of growing up. If these are broken then the last line of defense is the mid-March lows around 1257. If they're broken then it's a bit late to begin to notice the failure.

For now there still are many positives to look at. Even outside of the March 19th explosion studies that will be falling off the board, there are several more that make the bullish case. These include Trend Over Volatility, the High Put/Call, the 3 Surge Days and sharp drop in Consumer Sentiment. There is no need to overreact to the negative inferences of the April 11th market action. It is simply the first intermediate-term caution flag we've seen in the last month. It should be respected and we'll need to keep a close watch on further action. For now, I am moving the overall bias to neutral. I will therefore be willing to take both longs and shorts equally.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Trades

none

Open Big 50 Trades

None

Open Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 0

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

Index	ETF	CBI %	Index	ETF	CBI %
DJ US Broker Dealers	IAI	0.00	DJ US Energy	IYE	0.00
DJ US Insurance Index	IAK	1.35	DJ US Financial	IYF	0.68
DJ US Regional Banks	IAT	1.25	DJ US Financial Services	IYG	0.70
DJ US Utilities	IDU	0.00	DJ US Healthcare	IYH	0.00
DJ US Oil&Gas Expl & Prod	IEO	0.00	DJ US Industrial Sector	IYJ	0.00
DJ US Oil Equip & Svcs	IEZ	0.00	DJ US Consumer Goods	IYK	0.00
DJ US Pharmaceuticals	IHE	0.00	DJ US Basic Materials	IYM	1.35
DJ US Healthcare Providers	IHF	0.00	DJ US Real Estate	IYR	1.22
DJ US Medical Devices	IHI	2.44	DJ US Transportation	IYT	0.00
DJ US Aerospace & Defense	ITA	0.00	DJ US Technology Sector	IYW	0.50
DJ US Home Construction	ITB	0.00	DJ US Telecommunications	IYZ	0.00
DJ US Consumer Svcs	IYC	0.44	Nasdaq 100	QQQQ	0.00

No signs of capitulative selling at the present time.

Additional New Trade Ideas

none

Additional Trades Active Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SLB	4/8/2008	\$90.58	\$94.80	-4.7%		cover on close < 10ma
GRMN	4/11/2008	\$45.25	\$43.22	-4.5%		
MSFT	4/15/2008	\$28.06	\$29.00	3.3%		<i>sold @ \$29.00</i>

MSFT was sold for a nice quick gain. GRMN and SLB's action have disappointed so far.

Stocks and ETF's on my Radar

***Strong Selloffs In Congestion – now bouncing and could be shortable soon
AXP, WFR, WM, RIMM, AMZN, ATI, UTX.***

Notable S&P 500 stocks outside my “tradable” radar

Oversold

None

Overbought

None

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