QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 20, 2008 Issue 193

Market Overview

Summary of Recent Active Studies (see http://QuantifiableEdges.blogspot.com or Letters from listed dates for details)

Study Date	Description	Time span	Bias	Avg Max Move	Avg MM + 1 Std Dev
November 20, 2008	5% Drops	1-4 days	Bullish	5.28%	8.43%
November 20, 2008	Up Issues % 10ema < 30	1-5 days	Bullish	4.50%	7.78%
November 18, 2008	***2 Days Down in Chop***	***1-2 days***	***Bullish***	***1.50%***	***3.20%***
November 14, 2008	S&P Rises 2% and Spyx > 80	1-6 days	Bullish	3.40%	5.80%
March 17, 2008	Consumer Sentiment Stretch	1-12 months	Bullish		

If the avg max move is achieved it will appear in **bold and brown**. If the avg + 1 std deviation is achieved, the study will in ***bold italic blue*** and will be removed tomorrow.

Short-term Outlook (1-5 days) – somewhat bullish – updated 11/20

Another bloodletting on Wednesday. The Dow dropped 5%, the Nasdaq 6.5%, the S&P 6% and the Russell 2000 almost 8%. Volume came in higher than yesterday but just near average. The most lopsided statistics came when looking at breadth. Around 93% of all NYSE issues declined and close to 98% of the volume was down volume. The down volume was especially notable. Only the 8% drop on September 29th saw a larger percentage of down volume during this entire bear market.

As far as one-day selloffs go, between 1960 and 1987 the S&P never had a 5% drop. Between 1987 and August of 2008 it happened 8 times. In the last 2 months this is now the 9th drop in the S&P of 5% or greater. Earlier this month I did a study on these which suggested they're likely to rebound in the next few days. Since that time there have been 3 5% drops – 2 of which saw a rebound in the next few days an one that didn't.

The incredible down volume today took the 10-day EMA of the Up Volume % below 30. The last time the selling got so lopsided that it dropped below 30 was October 7th. Below is a study I ran looking at all the times since 1970 the Up Volume % 10-day ema dropped below 30:

Up Volume % 10-day EMA crosses below .30. Buy SPX on close. Sell X bars later. $100k/trade. 1970-present.												
X Days	*Net Profit*	*Trades*	*Wins*	*Losses*	*% Wins*	*Max Win*	*Max Loss*	*Avg Win*	*Avg Loss*	*W/L Ratio*	*Profit Factor*	*Avg Trade*
5	$38,351.10	17	13	4	76.47	$12,331.51	($12,167.91)	$4,558.84	($5,228.46)	0.87	2.83	$2,255.95
4	$25,132.13	18	14	4	77.78	$10,588.68	($12,157.32)	$3,198.12	($4,910.37)	0.65	2.28	$1,396.23
3	$8,680.10	19	11	8	57.89	$7,511.29	($9,701.00)	$3,395.18	($3,583.36)	0.95	1.30	$456.85
2	$1,600.67	20	11	9	55.00	$4,719.75	($16,188.58)	$2,922.79	($3,394.45)	0.86	1.05	$80.03
1	($15,495.51)	20	10	10	50.00	$3,816.80	($20,424.58)	$1,574.64	($3,124.19)	0.50	0.50	($774.78)

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No edge day 1, but 2-5 look pretty good. Notable is that the study would have triggered the day before the Crash of ’87, hence the 20% max loss on day 1.

In the trade ideas section below I show a new system. It’s one I unveiled at a presentation I gave tonight. Amazingly, tons of triggers hit today right on cue. The systems triggers page has FAR more triggers listed tonight than at any time since I began producing it a few weeks ago. Many of them are due to the new system, but even if I didn’t unveil it, there would have been a significant number of triggers. Among the ETF’s that triggered a long entry via system 81119 are SPY and QQQQ. There were also 2 new Catapult triggers tonight. That brings the CBI up to 6. Usually when the CBI starts building a sizable cluster like this I ignore all systems except Catapults. I do like to see what else is triggering though. On nights like tonight when there is a huge number of triggers suggesting a long or short bias, I do consider what it is telling me. I refer to this as “System Trigger Breadth” and it’s quite bullish now.

The Aggregator chart is updated below:

The Aggregator chart is in a bullish formation. The green Aggregator line is above 0 at 0.13, suggesting the S&P is likely to move higher over the next few days. The black differential line shows that the S&P has severely underperformed expectations over the last 3 days. Normally with such a formation I’d be gun-ho to get in at the open. My hesitation to go long just yet stems from the fact that we are just emerging from a consolidation and breaking down. I’ve mentioned in the past how I typically avoid rushing in to play a reversal when a security or index is in the process of breaking out or breaking down. Risks are much higher in such a situation because the break can feed upon itself and gain momentum quickly. My strong preference is to look for reversals when the stock or index is already stretched – both via the indicators and via the eyes.

Therefore, rather than look to enter near the open as I would normally do with such bullish studies in a short-term oversold market, I'll instead look to get long tomorrow at the close should the market continue to head lower. That would give us 2 lower closes in a row, which would trigger the chop system, and I've little doubt we'd see more extremes suggesting a likely reversal should we get another day down. Details in the trade idea section.

Intermediate-term Outlook (1 week – 2 months)–somewhat bullish -updated 11/17

New bear market lows were made this past week as the market has been unable to mount any kind of sustained move higher in the last few months.

Thursday's reversal set up the possibility that several divergences are emerging as the market is trying to hammer out a bottom. One such divergence which can easily be seen on the charts page is the Net New Highs. There are substantially less new 52-week lows on the NYSE than there were at the October low. While many technicians may point to this as a positive divergence, my March study showed no evidence of that. We've seen it happen a few times since then without success as well.

In the past I've shown some short-term trading systems based on "time stretches". Basically when price spends an extended period of time below a moving average, it tends to revert and rally back above it. I typically use it with regards to short-term moving averages like the 10-day. At this point there is a 200-day moving average time stretch that is in notable territory, though.

It has now been 225 days since the S&P last closed above its 200-day moving average. Looking back to 1960 there have only been 5 other instances where the S&P remained below the 200ma for this long. Buying on the 225th day and then selling when it crossed back above the 200-day moving average would have resulted in a winning trade every time, with an average gain of 6%.

Unfortunately this market has showed us time and again that it is unlike anything we've seen over at least that amount of time. Therefore I once again used the Dow to look and see how the strategy would have worked in the 1930's. After slicing through the 200 during the early part of the crash of '29 the market totaled 225 days below it on 9/15/30. Buying at that point would have been a disaster. It stayed below the 200ma until 8/22/32. Over that nearly 2-year period from the entry point it lost just over 70%.

One of the things that had me looking for an index reversal a little too early in October was the "mini-crash" on September 29th. Drops of that magnitude have either marked the bottom (1987) or led to a temporary bottom that the market would rally off with in a few weeks. Such was the case with many of the sharp drops between 1929 and 1932. In all those cases a rally emerged that lasted at least a month or so and gained at least 16%.

While we have not had a sustainable rally, there have been two sizable ones since early October. From the low on October 10th to the high on October 14th the S&P rallied over 24%. From the low on 10/28 to the high on 11/4 the market rallied over 19%. The 2nd one was the longest – 6 trading sessions. So while we haven't had a sustainable rally and lower prices were seen after both of these two, they did meet the requirements from a percent change standpoint. Have they simply been condensed versions of they rallies of the past? Or is a more sustainable rally lasting a few weeks to a few months still likely to occur?

It's unclear at this point, but I'm still of the opinion that the market is more likely to launch a substantial move higher form here than a substantial move lower. That's not to say we won't roll right back over after rallying for a month or two. But even if we get another quick leg down here, it would seem unlikely to me that the market won't be trading quite a bit higher between now and the end of the year.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Trades

IP - bought @ $11.77 limit (now out although the signal is officially still active)
CBS – bought @ $6.07 limit (now out although the signal is officially still active)
GD – @ $53.51
GD - @ $53.24

New

GD – buy 1/3 position @ 49.25 limit – 3rd and FINAL entry
F - @ $1.26 – ***This is NOT an official trade idea. I have NO interest in gambling with this possible bankruptcy candidate. I will monitor it for purposes of calculating the CBI.***

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 6/4 (IP, CBS, GD-3, F)

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

Not updated tonight

Index	ETF	CBI %		Index	ETF	CBI %
DJ US Broker Dealers	IAI	0.00		DJ US Energy	IYE	5.81
DJ US Insurance Index	IAK	2.70		DJ US Financial	IYF	3.08
DJ US Regional Banks	IAT	0.00		DJ US Financial Services	IYG	1.40
DJ US Utilities	IDU	0.00		DJ US Healthcare	IYH	10.56
DJ US Oil&Gas Expl & Prod	IEO	3.45		DJ US Industrial Sector	IYJ	10.34
DJ US Oil Equip & Svcs	IEZ	9.62		DJ US Consumer Goods	IYK	13.61
DJ US Pharmaceuticals	IHE	2.70		DJ US Basic Materials	IYM	4.05
DJ US Healthcare Providers	IHF	16.33		DJ US Real Estate	IYR	6.10
DJ US Medical Devices	IHI	12.20		DJ US Transportation	IYT	4.76
DJ US Aerospace & Defense	ITA	11.11		DJ US Technology Sector	IYW	9.55
DJ US Home Construction	ITB	9.52		DJ US Telecommunications	IYZ	2.63
DJ US Consumer Svcs	IYC	12.72		Nasdaq 100	QQQQ	5.00

Additional New Trade Ideas

GD – buy 1/3 position @ $49.25 limit. From Catapult section above

SPY – *buy ¼ index position on* ***close*** *@ $81.50 limit.* Based on short-term market outlook above. Looking to start scaling in should the market continue its freefall tomorrow.

Unofficial trade ideas

Below is system 81119. Results look at our list of 120 highly liquid ETF's for the last 10-years. See systems trigger page for a list of all securities in our watchlists that triggered this and other systems today.

ETF closes under 10-day moving average for 10 days in a row.			
ETF closes above its 200ma or at 50-day low.			
ETF suffers worst drop in last 10 days.			
Buy on close. Sell on close > 10-day moving average.			
Trades	615		
Wins	456		
Losses	156		
Pct Wins	**74.1%**		
Avg Win	4.2%		
Avg Loss	-3.8%		
Avg Trade	**2.2%**		
Profit Factor	3.23		

Active Trades Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
GD	11/18/2008	$53.51	$49.25	-7.96%		Catapult
GD	11/19/2008	$53.24	$49.25	-7.49%		Catapult
SPY	11/18/2008	$85.15	$85.39	0.28%	see below	sold

SPY was sold as detailed in this morning's Intraday Update – ½ @ $85.95 and ½ @ $84.83. Average price of $85.39 reflected above on the closed position.