

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

December 23, 2008

Issue 215

## 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
<b>Active</b>					
December 23, 2008	Santa Rally	1-5 days	Bullish	1.90%	3.60%
December 23, 2008	Late day surge	1 day	Bearish	-1.70%	-3.00%
December 22, 2008	Nasdaq Volume Spyx < -5	1-6 days	Bearish	-4.50%	-9.20%
March 17, 2008	Consumer Sentiment Stretch	1-12 months	Bullish		
<b>Dropped Tonight</b>					
December 17, 2008	S&P up 4% on mediocre volume	1-4 days	Bearish	-5.70%	-10.60%
December 10, 2008	SOX Up SPX Down	1-8 days	Bullish	5.70%	9.10%

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) –slightly bullish – updated 12/23**

The market fell hard for much of the day on Monday. A late day rally improved the numbers a bit, but it was still solidly down all around. The S&P 500, Nasdaq, and Russell 2000 all closed down by close to 2%. Breadth was poor. Advancers outnumbered decliners by about 3 to 1 and down volume led up volume by over 4 to 1. Overall volume fell to the lowest level since the shortened trading session the day after Thanksgiving.

The late-day surge triggered a study that appeared on the blog on October 31<sup>st</sup>. The study looked at times the market rose at least 0.75% in the last ten minutes of trading. Since the study there have been 6 instances. Three of which have gone against the previous results and moved higher rather substantially. Below is an updated performance report of the SPX based on buying the close after a 0.75% surge in the last 10 minutes of trading:

#### All Trades

Total Net Profit	(\$2,053.53)	Profit Factor	0.89
Gross Profit	\$15,974.92	Gross Loss	(\$18,028.45)
Total Number of Trades	18	Percent Profitable	27.78%
Winning Trades	5	Losing Trades	13
Even Trades	0		
Avg. Trade Net Profit	(\$114.09)	Ratio Avg. Win:Avg. Loss	2.30
Avg. Winning Trade	\$3,194.98	Avg. Losing Trade	(\$1,386.80)
Largest Winning Trade	\$6,420.72	Largest Losing Trade	(\$4,142.00)
Max. Consecutive Winning Trades	2	Max. Consecutive Losing Trades	5
Avg. Bars in Winning Trades	79.00	Avg. Bars in Losing Trades	79.00

The losing percentage is still notable. The average trade flattened out quite a bit thanks to the oversized gains seen in a few recent trades. Below is an updated list of all the trades.

Date/Time	Signal	Price	Roll Over USD/Lot	Shares/Ctrts Profit	Net Profit	Cum Net Profit	% Profit
06/20/86 16:00	Buy	\$247.60	\$0.00	403	(\$943.02)		(0.95%)
06/23/86 16:00	Sell	\$245.26			(\$943.02)	(\$943.02)	
12/19/86 16:00	Buy	\$249.27	\$0.00	401	(\$208.52)	(\$208.52)	(0.21%)
12/22/86 16:00	Sell	\$248.75			(\$208.52)	(\$1,151.54)	
12/04/87 16:00	Buy	\$223.87	\$0.00	446	\$2,180.94	\$2,180.94	2.18%
12/07/87 16:00	Sell	\$228.76			\$2,180.94	\$1,029.40	
01/02/90 16:00	Buy	\$359.69	\$0.00	278	(\$258.54)	(\$258.54)	(0.26%)
01/03/90 16:00	Sell	\$358.76			(\$258.54)	\$770.86	
08/22/97 16:00	Buy	\$923.55	\$0.00	108	(\$615.60)	(\$615.60)	(0.62%)
08/26/97 09:35	Sell	\$917.85			(\$615.60)	\$155.26	
09/24/98 16:00	Buy	\$1,041.67	\$0.00	95	(\$188.10)	(\$188.10)	(0.19%)
09/25/98 16:00	Sell	\$1,039.69			(\$188.10)	(\$32.84)	
04/14/00 16:00	Buy	\$1,356.56	\$0.00	73	\$3,282.81	\$3,282.81	3.32%
04/17/00 16:00	Sell	\$1,401.53			\$3,282.81	\$3,249.97	
07/15/02 16:00	Buy	\$917.87	\$0.00	108	(\$1,828.44)	(\$1,828.44)	(1.84%)
07/16/02 16:00	Sell	\$900.94			(\$1,828.44)	\$1,421.53	
08/08/07 16:00	Buy	\$1,497.49	\$0.00	66	(\$2,930.40)	(\$2,930.40)	(2.96%)
08/09/07 16:00	Sell	\$1,453.09			(\$2,930.40)	(\$1,508.87)	
10/13/08 16:00	Buy	\$1,003.35	\$0.00	99	(\$528.66)	(\$528.66)	(0.53%)
10/14/08 16:00	Sell	\$998.01			(\$528.66)	(\$2,037.53)	
10/20/08 16:00	Buy	\$985.40	\$0.00	101	(\$3,065.35)	(\$3,065.35)	(3.08%)
10/21/08 16:00	Sell	\$955.05			(\$3,065.35)	(\$5,102.88)	
10/28/08 16:00	Buy	\$940.51	\$0.00	106	(\$1,104.52)	(\$1,104.52)	(1.11%)
10/29/08 16:00	Sell	\$930.09			(\$1,104.52)	(\$6,207.40)	
10/30/08 16:00	Buy	\$954.09	\$0.00	104	\$1,524.64	\$1,524.64	1.54%
10/31/08 16:00	Sell	\$968.75			\$1,524.64	(\$4,682.76)	
11/07/08 16:00	Buy	\$930.99	\$0.00	107	(\$1,260.46)	(\$1,260.46)	(1.27%)
11/10/08 16:00	Sell	\$919.21			(\$1,260.46)	(\$5,943.22)	
11/13/08 16:00	Buy	\$911.29	\$0.00	109	(\$4,142.00)	(\$4,142.00)	(4.17%)
11/14/08 16:00	Sell	\$873.29			(\$4,142.00)	(\$10,085.22)	
11/21/08 16:00	Buy	\$800.03	\$0.00	124	\$6,420.72	\$6,420.72	6.47%
11/24/08 16:00	Sell	\$851.81			\$6,420.72	(\$3,664.50)	
12/02/08 16:00	Buy	\$848.81	\$0.00	117	\$2,565.81	\$2,565.81	2.58%
12/03/08 16:00	Sell	\$870.74			\$2,565.81	(\$1,098.69)	
12/16/08 16:00	Buy	\$913.18	\$0.00	109	(\$954.84)	(\$954.84)	(0.96%)
12/17/08 16:00	Sell	\$904.42			(\$954.84)	(\$2,053.53)	
12/22/08 16:00	Buy	\$871.63		114	n/a	n/a	n/a
open	n/a	\$871.63		n/a	n/a	n/a	n/a

With only two trading sessions left until Christmas, we are now in a seasonally strong period for the market. Below is a breakdown of the last 21 years and how the S&P has performed from this point forward.

<i>Buy at the close 3 trading sessions before Christmas. Sell X days later. \$100k/trade. 1987-present.</i>											
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade	
10	\$24,216.38	21	15	6	71.43	\$2,567.15	(\$2,381.81)	1.08	2.69	\$1,153.16	
9	\$29,032.24	21	14	7	66.67	\$2,950.08	(\$1,752.70)	1.68	3.37	\$1,382.49	
8	\$35,543.70	21	15	6	71.43	\$2,734.21	(\$911.58)	3.00	7.50	\$1,692.56	
7	\$25,120.32	21	14	7	66.67	\$2,225.08	(\$861.54)	2.58	5.17	\$1,196.21	
6	\$20,784.34	21	14	7	66.67	\$1,957.88	(\$946.57)	2.07	4.14	\$989.73	
5	\$26,695.32	21	16	5	76.19	\$1,923.08	(\$814.81)	2.36	7.55	\$1,271.21	
4	\$19,613.70	21	14	7	66.67	\$1,828.99	(\$856.03)	2.14	4.27	\$933.99	
3	\$15,416.38	21	13	8	61.90	\$1,622.68	(\$709.81)	2.29	3.71	\$734.11	
2	\$14,473.02	21	16	5	76.19	\$1,131.76	(\$727.01)	1.56	4.98	\$689.19	
1	\$9,813.28	21	16	5	76.19	\$776.69	(\$522.74)	1.49	4.75	\$467.30	

The next 1 to 5 days has been especially bullish. If you decided to buy the close 3 sessions before Christmas and then sell the 1<sup>st</sup> profitable close after entry then 18 of 21 trades would have been winners within 2 days and 20 of 21 within 5 days.

As I discussed a little over a week ago smallcaps have a tendency to outperform this time of year. So rather than just look at the S&P 500 I also looked at the Russell 2000 and the Nasdaq Composite. These indices both help provide a smaller cap view. For both indices buying the close 3 sessions before Christmas and then selling the 1<sup>st</sup> profitable exit would have resulted in 100% (21 of 21) winning trades within four days of entry. In fact, in the history of the Nasdaq if you gave the trade through the 1<sup>st</sup> trading day of the New Year to work you would have been profitable all 37 years. The only instance that took longer than 5 days was 1986.

One concern that remains is that the VIX is still extended to the downside. As we've seen in recent studies this suggests that upside may be limited in the coming days.

I have updated the [Aggregator](#) chart below:



The green Aggregator line rose sharply today and is now slightly above the 0 line and in neutral territory. Meanwhile, the black differential line is strongly above 0 indicating the market has strongly underperformed expectations over the last few days. Not ideal as I'd rather see a stronger reading from the Aggregator, but still good enough for toe-dipping. I'm going to look to begin putting on a QQQQ position. I'm favoring the QQQQ since it is oversold about the same amount but seasonally has done a little better.

***Intermediate-term Outlook (2 weeks – 2 months)– very slightly bullish -updated 12/22***

The market has stumbled higher off its mid-November lows. Some key ingredients for an intermediate-term rally were in place as I discussed at the time. These included extremely oversold conditions followed by sharp rallies higher and bullish divergences. The pullbacks have been fairly mild and the market has worked its way higher.

Notable this week was that the S&P closed above its 50-day moving average for the first time in a long time. I posted a study on the blog a few days ago that looked at other times the S&P had spent a long time below its 50 and then moved above it. The results suggested a trading range was more likely than a strong market move in either direction. Results were also slightly bullish.

Last week I noted the Nasdaq had so far failed to take on a leadership role. This is a bit concerning since the market has achieved over 100% of its gains in the last 38 years while the Nasdaq was leading. As you can see below, the Nasdaq has still failed to take on a leadership role (relative strength line that the bottom is red).



This weekend I looked at other times the market has come off an intermediate-term bottom and after five weeks the Nasdaq had still failed to take on a leadership role. Surprisingly, results were not materially different from those where the Nasdaq quickly began to lead.

I also noticed that it was not only the daily Nasdaq Volume Spyx that posted an extreme reading Friday, but the weekly Nasdaq Volume Spyx closed extremely low as well. I've included a chart of it below:



The 0.61 reading is exceptionally low. I ran a test back to 2000 to see how the Nasdaq performed following readings below 10:

Nas Spyx Weekly closes below 10.										
Buy on close. Sell X days later. \$1mil/trade. 2000-present. (One entry at a time.)										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
13	(\$69,942.29)	9	4	5	44.44	\$91,331.55	(\$87,053.70)	1.05	0.84	(\$7,771.37)
12	\$48,468.49	9	4	5	44.44	\$94,100.62	(\$65,586.80)	1.43	1.15	\$5,385.39
11	\$167,927.75	9	4	5	44.44	\$108,411.96	(\$53,144.02)	2.04	1.63	\$18,658.64
10	\$130,824.68	10	6	4	60.00	\$64,729.34	(\$64,387.83)	1.01	1.51	\$13,082.47
9	(\$58,162.56)	12	6	6	50.00	\$74,164.03	(\$83,857.79)	0.88	0.88	(\$4,846.88)
8	(\$139,047.47)	12	6	6	50.00	\$54,592.55	(\$77,767.13)	0.70	0.70	(\$11,587.29)
7	(\$112,341.13)	13	5	8	38.46	\$47,663.04	(\$43,832.04)	1.09	0.68	(\$8,641.63)
6	(\$177,179.20)	13	4	9	30.77	\$59,619.19	(\$46,184.00)	1.29	0.57	(\$13,629.17)
5	(\$261,007.76)	14	4	10	28.57	\$56,164.53	(\$48,566.59)	1.16	0.46	(\$18,643.41)
4	(\$267,695.62)	14	5	9	35.71	\$42,002.62	(\$53,078.75)	0.79	0.44	(\$19,121.12)
3	(\$28,192.81)	16	8	8	50.00	\$46,429.31	(\$49,953.41)	0.93	0.93	(\$1,762.05)
2	(\$111,156.21)	18	8	10	44.44	\$40,635.74	(\$43,624.21)	0.93	0.75	(\$6,175.35)
1	(\$33,565.97)	22	10	12	45.45	\$23,571.01	(\$22,439.67)	1.05	0.88	(\$1,525.73)

These numbers look a bit bigger than most tests because it was run using a \$1mil/trade instead on \$100k. The Nasdaq has struggled over the following five weeks or so by a fairly sizable amount.

For most tests I only allow one entry at a time. This way there is no double-counting on certain weeks. Sometimes I'll run them and allow multiple positions to be active at one time. I decided to do that here and have posted those results below:

<b>Nas Spyx Weekly closes below 10.</b>										
<b>Buy on close. Sell X days later. \$1mil/trade. 2000-present. (Multiple entries at a time.)</b>										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
13	(\$781,862.96)	22	7	15	31.82	\$85,053.99	(\$91,816.06)	0.93	0.43	(\$35,539.23)
12	(\$613,187.24)	22	8	14	36.36	\$77,306.95	(\$87,974.49)	0.88	0.50	(\$27,872.15)
11	(\$416,236.65)	22	7	15	31.82	\$105,589.40	(\$77,024.17)	1.37	0.64	(\$18,919.85)
10	(\$377,068.42)	22	9	13	40.91	\$75,966.77	(\$81,597.64)	0.93	0.64	(\$17,139.47)
9	(\$228,620.32)	22	10	12	45.45	\$72,780.38	(\$79,702.01)	0.91	0.76	(\$10,391.83)
8	(\$290,904.91)	22	10	12	45.45	\$56,955.03	(\$71,704.60)	0.79	0.66	(\$13,222.95)
7	(\$147,928.86)	22	8	14	36.36	\$53,951.24	(\$41,395.63)	1.30	0.74	(\$6,724.04)
6	(\$265,528.77)	22	7	15	31.82	\$58,952.31	(\$45,212.99)	1.30	0.61	(\$12,069.49)
5	(\$343,882.18)	22	7	15	31.82	\$56,905.58	(\$49,481.42)	1.15	0.54	(\$15,631.01)
4	(\$421,294.95)	22	8	14	36.36	\$45,679.29	(\$56,194.95)	0.81	0.46	(\$19,149.77)
3	(\$197,222.46)	22	10	12	45.45	\$43,699.31	(\$52,851.29)	0.83	0.69	(\$8,964.66)
2	(\$154,309.00)	22	10	12	45.45	\$38,003.11	(\$44,528.34)	0.85	0.71	(\$7,014.05)
1	(\$33,565.97)	22	10	12	45.45	\$23,571.01	(\$22,439.67)	1.05	0.88	(\$1,525.73)

Results appear even more negative here. This isn't surprising considering there are some bad weeks that are being double counted.

Overall, the market is still stair-stepping it way higher. We're near a seasonally bullish time of year. The government has indicated it is going to do whatever it takes to get the economy moving again. Aside from the Nasdaq Volume Spyx readings I'm not seeing much that would suggest a selloff is imminent. It does appear unlikely that the market is just going to blast off from here, though. Right now a range bound scenario appears the most likely to me. If forced to pick a direction beyond a few weeks, I'd likely lean bullish.

### **Catapult and Capitulative Breadth Statistics**

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

#### ***Open Catapult Trades***

none

#### ***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	0.00	DJ US Financial	IYF	0.34
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	0.38
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	0.00
DJ US Healthcare Providers	IHF	0.00	DJ US Real Estate	IYR	0.00
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	0.00
DJ US Home Construction	ITB	0.00	DJ US Telecommunications	IYZ	0.00
DJ US Consumer Svcs	IYC	0.00	Nasdaq 100	QQQQ	0.00

*No capitulative action evident.*

### **Additional New Trade Ideas**

*QQQQ –buy 1/4 index position @ \$29.06 limit.* Based on short-term overview. Since the setup isn't ideal, and the Aggregator is weaker than I normally demand I'll look to buy on a slight retracement of Monday's weakness. I'll also likely look for a quick profit if it closes higher in the next day or two.

### **Active Trades Table**

Symbol	Entry Date	Entry Price	Current Pr	% Gain/Lo	Stop	Notes
IEF(s)	12/19/2008	\$99.85	\$99.26	0.59%		cover on close < 10ma

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