# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 13, 2009 Volume 2 Issue 8

## 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 |
|---|---|---|---|---|---|
| Active | | | | | |
| January 13, 2009 | 2 Down In Chop | 1-3 days | Bullish | 1.65% | 3.50% |
| January 9, 2009 | NDX 1% while SOX down | 1-6 days | Bearish | -4.70% | -9.60% |
| January 5, 2009 | Appel Breadth Thrust | 1-20 days | Bullish | 3.70% | 5.70% |
| ***December 31, 2008*** | ***10/200 Put/Call < 0.85*** | ***1-9 days*** | ***Bearish*** | ***-2.70%*** | ***-5.00%*** |
| December 29, 2008 | 10/100 ATR < 0.60 | n/a | Bearish | n/a | n/a |
| Active - Long Term | | | | | |
| December 18, 2008 | Break above 50-day | | Neutral - Trading Range | | |
| December 21, 2008 | Nasdaq Lagging | | Bearish | | |
| December 21, 2008 | Nasdaq Vol Spyx Low | 1-5 weeks | Bearish | | |
| March 17, 2008 | Consumer Sentiment Stretch | 1-12 months | Bullish | | |
| Dropped Tonight | | | | | |
| ***January 8, 2009*** | ***Gap n Crap From Sht Term Ovr*** | ***1-3 days*** | ***Bearish*** | ***-2.70%*** | ***-5.20%*** |
| January 8, 2009 | 2.5% - 5% Declines In Bear | 1-3 days | Bearish | -4.96% | -9.70% |

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***.

***Short-term Outlook (1-5 days) –neutral approaching bullish – updated 01/13***

The market followed up Friday's losses with more selling on Monday. The major indices were all down 1.5% or more. NYSE declining issues outnumbered advancers by over 3 to 1 and down volume beat up volume by almost 9 to1. Volume overall declined for the 4th day in a row.

I looked at the low volume a few different ways tonight. For one I looked at patterns of back to back 1% down days. I compared times when the volume shrunk both days to times it didn't. I also looked at performance following 2-period RSI readings of below 10 . In this case I compared times when the volume made a 5-day low to times it didn't. Neither set of tests suggested today's light volume provided a substantial edge – either bullish or bearish.

Somewhat notable today was that the VIX and VXO crossed and closed more than 10% above their 10-day moving averages. Many traders consider a stretch of 10% or more to be short-term bullish. I ran a test based on this concept below:

| VXO crosses above its 10-day moving average. The S&P 500 closes under its 200-day moving average. | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Buy S&P 500 on close. Sell X days later. $100k/trade. 1988 - present. | | | | | | | | | | |
| X Day of Wk | Net Profits | Trades | Wins | Losses | % Wins | Avg Win | Avg Loss | W/L Ratio | Profit Factor | Avg Trade |
| 8 | $22,818.21 | 66 | 35 | 31 | 53.03 | $3,067.43 | ($2,727.16) | 1.12 | 1.27 | $345.73 |
| 7 | $34,061.30 | 71 | 34 | 37 | 47.89 | $3,411.77 | ($2,214.57) | 1.54 | 1.42 | $479.74 |
| 6 | $2,174.74 | 75 | 37 | 38 | 49.33 | $2,660.48 | ($2,533.23) | 1.05 | 1.02 | $29.00 |
| 5 | $24,239.58 | 80 | 41 | 39 | 51.25 | $2,491.40 | ($1,997.64) | 1.25 | 1.31 | $302.99 |
| 4 | $18,874.31 | 83 | 40 | 43 | 48.19 | $2,273.66 | ($1,676.09) | 1.36 | 1.26 | $227.40 |
| 3 | $11,918.13 | 88 | 47 | 41 | 53.41 | $1,869.71 | ($1,852.64) | 1.01 | 1.16 | $135.43 |
| 2 | $17,035.41 | 96 | 45 | 51 | 46.88 | $2,024.48 | ($1,452.28) | 1.39 | 1.23 | $177.45 |
| 1 | $9,622.22 | 96 | 50 | 46 | 52.08 | $1,217.77 | ($1,114.48) | 1.09 | 1.19 | $100.23 |

If there is an edge in this setup it's very small. I'd prefer to see the VXO either spike even higher or to remain elevated for several days before I'd consider it a strong enough edge to take positions.

Notable from a long-term system standpoint is that the Appel Breadth thrust signal discussed in last Monday's letter triggered an unprofitable exit today after only 6 days.

One system that did trigger tonight was the "2 Days Down In Chop" system. This system looks to get long any time the S&P closes lower 2 days in a row and then exits at the 1st profitable close up to 3 days later. On the 3rd day it will exit regardless. It has been especially effective since the market became more choppy in June of 2007. Results for 6/1/2007 – present are below:

| All Trades | | | |
|---|---|---|---|
| Total Net Profit | $40,494.07 | Profit Factor | 2.73 |
| Gross Profit | $63,926.81 | Gross Loss | ($23,432.74) |
| Total Number of Trades | 50 | Percent Profitable | 88.00% |
| Winning Trades | 44 | Losing Trades | 6 |
| Even Trades | 0 | | |
| Avg. Trade Net Profit | $809.88 | Ratio Avg. Win:Avg. Loss | 0.37 |
| Avg. Winning Trade | $1,452.88 | Avg. Losing Trade | ($3,905.46) |
| Largest Winning Trade | $10,716.03 | Largest Losing Trade | ($10,506.45) |
| Max. Consecutive Winning Trades | 17 | Max. Consecutive Losing Trades | 2 |

Very strong results, especially considering it took place almost entirely during the bear market. After a sizable loss at the beginning of October the system has reeled off 9 straight winners. The last 10 trades are listed below:

| Date/Time | Signal | Price | Roll Over USD/Lot | Shares/Ctrts Profit | Net Profit Cum Net Profit | % Profit |
|---|---|---|---|---|---|---|
| 10/02/08 | Buy | $1,114.28 | $0.00 | 89 | ($10,506.45) | (10.59%) |
| 10/07/08 | Sell | $996.23 | | ($10,506.45) | $11,907.45 | |
| 10/15/08 | Buy | $907.84 | $0.00 | 110 | $4,244.90 | 4.25% |
| 10/16/08 | Sell#2 | $946.43 | | $4,244.90 | $16,152.35 | |
| 10/22/08 | Buy | $896.78 | $0.00 | 111 | $1,257.63 | 1.26% |
| 10/23/08 | Sell#2 | $908.11 | | $1,257.63 | $17,409.98 | |
| 10/27/08 | Buy | $848.92 | $0.00 | 117 | $10,716.03 | 10.79% |
| 10/28/08 | Sell#2 | $940.51 | | $10,716.03 | $28,126.01 | |
| 11/06/08 | Buy | $904.88 | $0.00 | 110 | $2,872.10 | 2.89% |
| 11/07/08 | Sell#2 | $930.99 | | $2,872.10 | $30,998.11 | |
| 11/11/08 | Buy | $898.95 | $0.00 | 111 | $1,369.74 | 1.37% |
| 11/13/08 | Sell#2 | $911.29 | | $1,369.74 | $32,367.85 | |
| 11/17/08 | Buy | $850.75 | $0.00 | 117 | $979.29 | 0.98% |
| 11/18/08 | Sell#2 | $859.12 | | $979.29 | $33,347.14 | |
| 11/20/08 | Buy | $752.44 | $0.00 | 132 | $6,281.88 | 6.32% |
| 11/21/08 | Sell#2 | $800.03 | | $6,281.88 | $39,629.02 | |
| 12/18/08 | Buy | $885.28 | $0.00 | 112 | $291.20 | 0.29% |
| 12/19/08 | Sell#2 | $887.88 | | $291.20 | $39,920.22 | |
| 12/23/08 | Buy | $863.16 | $0.00 | 115 | $573.85 | 0.58% |
| 12/24/08 | Sell#2 | $868.15 | | $573.85 | $40,494.07 | |
| 01/12/09 | Buy | $870.26 | | 114 | n/a | n/a |
| open | n/a | $870.26 | | n/a | n/a | |

I have updated the Aggregator chart below:


The black differential line remains very stretched. Still the green Aggregator line still hasn't quite made it back to positive territory. There are some bearish studies which still remain active and with breadth, sentiment, and volume failing to produce meaningful bullish edges we're really only relying on oversold price measures in a choppy environment to suggest a bullish edge. Oversold in chop is powerful and I believe a move higher is fairly likely here, but it's certainly no layup as is evidenced by the Aggregator line.

***Intermediate-term Outlook (2 weeks – 2 months)–very slightly bullish -updated 1/12/9***

This week's action did little to change current long-tem studies or to ignite new ones. Last week's breadth thrust failed to follow through as major indices pulled back 4% or more this week. Still it remains above recent swing lows which would equal about 860 in the S&P 500.

The study that's shown to be the most predictive among the long-term actives is the "Break above 50-day" which suggested a choppy trading range was more likely than a strong trend.

Last week I wrote "*between the price breakout and the breadth thrust there may be some hope for an intermediate-term rally. I'm slightly bullish right now and without further evidence that the rally is likely to fail I may begin to buy oversold conditions more aggressively than I short overbought ones*." The problem so far with this 1st pullback is that it has failed to reveal bullish edges. While I'd love to be able to get aggressive we remain in the unusual position of experiencing a selloff where bearish short-term studies continue to dominate.

If support levels fail to hold that could invalidate both the breadth thrust and the inverse head and shoulders breakout ideas from last week – effectively wiping out the bullish thesis for now. I'm keeping an eye on the 850-860 range and also looking to see whether study results come out bullish or bearish these next few days. This week could be a critical test of the upmove.

**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 | 0.00 |
| DJ US Regional Banks | IAT | 0.00 | | DJ US Financial Services | IYG | 0.00 |
| 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 | 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 | 5.26 |
| DJ US Consumer Svcs | IYC | 0.00 | | Nasdaq 100 | QQQQ | 0.00 |

*Nothing doing.*

## Additional New Trade Ideas

*SPY – Buy ¼ index position @ $87.04* ***limit on CLOSE****. The Aggregator isn't quite there, but another close lower tomorrow and I'll be looking to scale in. The lower close would likely generate some additional short-term bullish studies and that's what I'm anticipating.*

## Active Trades Table

None currently open.