QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 11, 2009 Volume 2 Issue 28

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					
February 11, 2009	Spyx Spikes 80+ points	1-2 days	Bullish	1.00%	1.90%
February 11, 2009	2.5% Drop Frim High	1-4 days	Bearish	-2.70%	-4.60%
February 10, 2008	**Low Nasdaq Spyx w/ Q RSI > 90**	**1-7 days**	**Bearish**	**-4.10%**	**-8.70%**
February 9, 2009	**1st Friday Up 1%**	**1-5 days**	**Bearish**	**-2.70%**	**-5.60%**
Active - Long Term					
February 9, 2009	Nasdaq Breadth Trhust	1-20 days	Bullish	5.90%	9.60%
March 17, 2008	Consumer Sentiment Stretch	1-12 months	Bullish		
Dropped Tonight					
February 10, 2008	***NR10 Low V 10 Under 200ma Hi 5***	***1-4 days***	***Bearish***	***-2.80%***	***-5.00%***
February 9, 2009	***Up 2.5%-5% During Bear***	***1-2 days***	***Bearish***	***-3.00%***	***-5.00%***
February 9, 2009	***2 Days Up In Chop***	***1-4 days***	***Bearish***		

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) – updated 2/11 – slightly bearish

The expected selloff arrived Tuesday in a big way. The major indices all dropped between 4% and 5%. Breadth was exceptionally weak. The NYSE Up Issues % came in at 15% and the Up Volume % was a mere 3%. Total volume expanded to the highest level in weeks, but it wasn't substantially higher than the volume seen last Thursday and Friday.

Looking at the charts page what stuck out to me was the tremendous moves up seen in the Volume Spyx readings. Both the S&P and Nasdaq saw their Spyx readings rise over 80 points. Below is a test that looks at such spikes in the past.

S&P 500 Volume Spyx closes over 80 points higher than yesterday.										
Buy on close. Sell X days later. $100k/trade. 1995 - 2/10/2009										
X Days	Net Profits	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Facto	Avg Trade
5	$21,349.50	33	21	12	63.64	$1,605.33	($1,030.20)	1.56	2.73	$646.95
4	$9,032.55	33	25	8	75.76	$1,040.64	($2,122.93)	0.49	1.53	$273.71
3	$13,455.54	33	24	9	72.73	$1,094.24	($1,422.92)	0.77	2.05	$407.74
2	$13,440.11	33	24	9	72.73	$834.83	($732.86)	1.14	3.04	$407.28
1	$10,937.50	33	21	12	63.64	$893.30	($651.81)	1.37	2.40	$331.44

There seem to be a bit of an upside edge over the next 2-3 days though certainly nothing huge.

So what happens after strong selloffs like we saw today? When we consider the potential influence an individual bar may have on future bars it is important to consider the positioning of the bar we are studying. A sharp selloff coming when the market is extended up has a whole different meaning than a sharp selloff when the market is extended down. Let's first look at the current situation to see what I'm talking about.

S&P 500 closes down over 3% today after closing at a 5-day high yesterday.												
Buy on close. Sell X days later. $100k/trade. 1960 - 2/10/2009												
X Days	Net Profits	Trades	Wins	Losses	% Wins	Max Win	Max Loss	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
5	($21,538.43)	11	3	8	27.27	$11,405.78	($10,448.88)	$5,013.39	($4,572.32)	1.10	0.41	($1,958.04)
4	($6,740.34)	11	3	8	27.27	$7,302.92	($5,597.28)	$2,950.63	($1,949.03)	1.51	0.57	($612.76)
3	($4,831.76)	11	6	5	54.55	$3,539.22	($4,002.90)	$995.27	($2,160.68)	0.46	0.55	($439.25)
2	$7,052.22	11	5	6	45.45	$6,652.66	($2,325.78)	$3,104.21	($1,411.47)	2.20	1.83	$641.11
1	$2,452.00	11	7	4	63.64	$5,394.60	($4,980.56)	$1,815.00	($2,563.26)	0.71	1.24	$222.91

Here we see the sharp 1-day selloff has typically led to a muted bounce that then rolls over to make new lows. Instances are quite low, though, so I loosened the requirements to 2.5%:

S&P 500 closes down over 2.5% today after closing at a 5-day high yesterday.												
Buy on close. Sell X days later. $100k/trade. 1960 - 2/10/2009												
X Days	Net Profits	Trades	Wins	Losses	% Wins	Max Win	Max Loss	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
5	($30,689.67)	20	6	14	30.00	$11,405.78	($10,448.88)	$3,310.38	($3,610.85)	0.92	0.39	($1,534.48)
4	($19,566.29)	20	4	16	20.00	$7,302.92	($5,597.28)	$3,370.60	($2,065.54)	1.63	0.41	($978.31)
3	($14,357.96)	20	8	12	40.00	$3,539.22	($4,002.90)	$976.27	($1,847.34)	0.53	0.35	($717.90)
2	($1,442.78)	20	7	13	35.00	$6,652.66	($5,656.78)	$2,391.37	($1,398.64)	1.71	0.92	($72.14)
1	($1,404.63)	20	12	8	60.00	$5,394.60	($4,980.56)	$1,137.05	($1,881.15)	0.60	0.91	($70.23)

Here we see more of the same. Many trades bounced in the 1st day or two before rolling over. To confirm further I loosened the requirements again to 2% and found more of the same there. Based on this the odds seem to favor further selling – perhaps after a short bounce.

But what if the market was at a 5-day low instead of a 5-day high yesterday? Results in that case would be much different:

S&P 500 closes down over 2.5% today after closing at a 5-day low yesterday.										
Buy on close. Sell X days later. $100k/trade. 1960 - 2/10/2009										
X Days	Net Profits	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
5	$104,909.07	42	28	14	66.67	$4,836.09	($2,178.68)	2.22	4.44	$2,497.84
4	$65,225.12	44	29	15	65.91	$3,988.84	($3,363.42)	1.19	2.29	$1,482.39
3	$64,503.48	45	27	17	60.00	$3,877.89	($2,364.69)	1.64	2.60	$1,433.41
2	$67,175.71	46	34	12	73.91	$3,164.67	($3,368.58)	0.94	2.66	$1,460.34
1	$41,093.95	49	34	15	69.39	$2,513.84	($2,958.44)	0.85	1.93	$838.65

Here we see a sharp initial bounce that is followed by more upside. The expectation turns from negative to positive based on where the sharp selloff is occurring. Since Tuesday's selloff occurred following a sizable move up these tests are suggesting more downside over the next 3-5 days.

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Tonight's Aggregator chart is below:

All of our bearish studies from the last few days reached at least as low as their average maximum move lower. Many even reached their average max move plus 1 standard deviation and are being removed. Along with tonight's studies this has caused the green Aggregator ling to curl back up, though it is still below the zero line. Meanwhile the sharp drop has caused the black differential line to cross back above zero. Without a strong bounce tomorrow the Differential line will continue to rise sharply.

A configuration like this where the black line crosses strongly through zero while we are in a position can often be an opportune time for profit taking. And we did take profits on most of the positions today. There is only one SPY lot remaining. The market therefore could move lower over the next few days. But with so many bearish studies already hitting their targets and the black differential line crossing above zero, any remaining downside edge is small. I am therefore of a mind to look for an opportunity to take profits on the remaining SPY position. I will outline my profit-taking targets and strategy in the Active Trade Ideas section below.

Intermediate-term Outlook (2 weeks – 2 months)–SLIGHTLY bullish -updated 2/9

One nice sign we've seen of late is the emerging leadership position of the Nasdaq relative to the NYSE. Below is a chart I sometimes refer to which shows the Nasdaq vs. NYSE relative strength:

I first discussed this indicator on the blog last February. Since the inception of the Nasdaq in 1971, close to 100% of the gains in the NYSE have come when the Nasdaq has been in a leadership position. The indicator is a bit controversial since part of the reason it works is due to the fact that the Nasdaq typically has a higher beta. In other words, it goes up more in up markets and down more in down markets. Since it goes up more in up markets it will often be in the lead when the NYSE is rising. Still, another possible reason this indicator works well is that is measures investors' appetite for risk. Nasdaq stocks have traditionally been riskier that NYSE stocks. When investors are more willing to take on that additional risk, it normally means good things for the stock market as a whole. In any event, the track record is good enough that it deserves a glance once in a while, and when its in a leading position as it is now I consider that a positive.

Another Nasdaq positive is that Nasdaq breadth has been especially strong lately. As can be seen on our charts page, the 10-day ema of the Nasdaq Up Volume % is now close to 64%. This is the highest level it has been at since the bear market began. The chart on that page uses Tradestation's data, which only goes back to 2000. To get a longer term look at the indicator I used Quotes Plus data, which goes back to 1/1/92. There are normally minor discrepancies between data sources when looking at breadth and volume data and Quotes Plus data currently puts the 10-day ema at almost 65%. The test below looks at breadth thrusts that move the ema above 64%:

Nasdaq Up Volume % 10-day ema crosses over 64%.										
Buy Nasdaq on close. Sell X days later. $100k/trade. 1992-2/6/2009										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
30	$75,056.27	19	13	6	68.42	$7,414.21	($3,554.75)	2.09	4.52	$3,950.33
20	$65,533.02	20	16	4	80.00	$5,134.87	($4,156.21)	1.24	4.94	$3,276.65
15	$51,774.69	23	15	8	65.22	$4,863.23	($2,646.72)	1.84	3.45	$2,251.07
10	$18,455.29	23	17	6	73.91	$1,742.47	($1,861.11)	0.94	2.65	$802.40
9	$27,723.57	23	16	7	69.57	$2,339.08	($1,385.95)	1.69	3.86	$1,205.37
8	$28,370.26	24	18	6	75.00	$2,136.44	($1,680.96)	1.27	3.81	$1,182.09
7	$16,080.32	24	15	9	62.50	$1,827.48	($1,259.10)	1.45	2.42	$670.01
6	$10,124.79	24	14	10	58.33	$1,949.10	($1,716.26)	1.14	1.59	$421.87
5	$4,087.16	24	12	12	50.00	$1,708.39	($1,367.79)	1.25	1.25	$170.30
4	$9,701.14	25	15	10	60.00	$1,637.33	($1,485.88)	1.10	1.65	$388.05
3	($1,260.22)	28	16	12	57.14	$1,643.20	($2,295.95)	0.72	0.95	($45.01)
2	($3,929.78)	29	18	11	62.07	$955.48	($1,920.77)	0.50	0.81	($135.51)
1	($7,608.66)	29	14	15	48.28	$731.38	($1,189.86)	0.61	0.57	($262.37)

A slight pullback has often been followed by bullish action. Rather than looking at just an exit of X days out, I also decided to use a drop in the 10-day ema as a possible exit as well. Below are the results of buying into an Up Volume % 10-day ema thrust above 64% and then holding until the indicator dips below X%:

Nasdaq Up Volume % 10-day ema crosses over 64%.										
Buy Nasdaq on close. Sell when Up Vol % ema crosses below X. $100k/trade. 1992-2/6/2009										
X% ema	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
0.44	$112,624.78	17	11	6	64.71	$11,798.99	($2,860.69)	4.12	7.56	$6,624.99
0.45	$105,842.15	18	11	7	61.11	$11,615.21	($3,132.17)	3.71	5.83	$5,880.12
0.46	$115,435.57	18	12	6	66.67	$11,197.13	($3,155.00)	3.55	7.10	$6,413.09
0.47	$118,500.16	18	12	6	66.67	$11,426.80	($3,103.56)	3.68	7.36	$6,583.34
0.48	$59,627.05	20	10	10	50.00	$8,273.10	($2,310.40)	3.58	3.58	$2,981.35
0.49	$37,459.30	21	10	11	47.62	$6,542.43	($2,542.27)	2.57	2.34	$1,783.78
0.5	$42,355.20	21	11	10	52.38	$6,250.12	($2,639.62)	2.37	2.60	$2,016.91

Making the exits too tight here reduced profitability greatly. Once the exit trigger dropped to 0.47 or below it appears to be fairly solid. Below is a more detailed performance report which enters on a move above 64% and uses the 47% number as the exit.

All Trades			
Total Net Profit	$126,672.37	Profit Factor	7.80
Gross Profit	$145,293.75	Gross Loss	($18,621.38)
Roll Over Credit	$0.00		
Open Position Profit/Loss	$0.00		
Select Total Net Profit	$126,672.37	Select Profit Factor	7.80
Select Gross Profit	$145,293.75	Select Gross Loss	($18,621.38)
Adjusted Total Net Profit	$77,127.53	Adjusted Profit Factor	3.94
Adjusted Gross Profit	$103,351.06	Adjusted Gross Loss	($26,223.53)
Total Number of Trades	18	Percent Profitable	66.67%
Winning Trades	12	Losing Trades	6
Even Trades	0		
Avg. Trade Net Profit	$7,037.35	Ratio Avg. Win:Avg. Loss	3.90
Avg. Winning Trade	$12,107.81	Avg. Losing Trade	($3,103.56)
Largest Winning Trade	$40,548.60	Largest Losing Trade	($4,386.96)
Largest Winner as % of Gross Profit	27.91%	Largest Loser as % of Gross Loss	23.56%

Most of the numbers here look outstanding. Twice as many winners as losers and the average win is nearly 4 times the average loss. This puts the profit factor at a gaudy 7.8. The one red flag on this report is the “largest winning trade”, which I circled above. This trade makes up nearly 28% of all the gross profits. So to more deeply analyze the results I’ve shown below the listing of al the individual trades.

#	Type	Date/Time	Signal	Price	Roll Over Pips	Shares/Ctrts Profit/Loss	Gross P/L Cum Net Profit	% Profit
1	Buy	10/16/92	Daily Breadth	$582.61	$0.00	171	$14,155.38	14.21%
	Sell	02/16/93	Sell	$665.39		$14,155.38	$14,155.38	
2	Buy	06/19/95	Daily Breadth	$922.09	$0.00	108	$12,523.68	12.58%
	Sell	09/26/95	Sell	$1,038.05		$12,523.68	$26,679.06	
3	Buy	04/25/96	Daily Breadth	$1,184.17	$0.00	84	$2,436.84	2.45%
	Sell	06/14/96	Sell	$1,213.18		$2,436.84	$29,115.90	
4	Buy	05/05/97	Daily Breadth	$1,339.24	$0.00	74	$24,243.14	24.46%
	Sell	10/17/97	Sell	$1,666.85		$24,243.14	$53,359.04	
5	Buy	11/02/98	Daily Breadth	$1,800.91	$0.00	55	$28,043.40	28.31%
	Sell	02/09/99	Sell	$2,310.79		$28,043.40	$81,402.44	
6	Buy	07/02/99	Daily Breadth	$2,741.02	$0.00	36	($4,386.96)	(4.45%)
	Sell	07/26/99	Sell	$2,619.16		($4,386.96)	$77,015.48	
7	Buy	11/16/99	Daily Breadth	$3,293.05	$0.00	30	$40,548.60	41.04%
	Sell	03/29/00	Sell	$4,644.67		$40,548.60	$117,564.08	
8	Buy	04/19/01	Daily Breadth	$2,182.04	$0.00	45	($3,364.20)	(3.43%)
	Sell	05/11/01	Sell	$2,107.28		($3,364.20)	$114,199.88	
9	Buy	11/13/01	Daily Breadth	$1,892.11	$0.00	52	$1,374.36	1.40%
	Sell	12/20/01	Sell	$1,918.54		$1,374.36	$115,574.24	
10	Buy	11/01/02	Daily Breadth	$1,360.70	$0.00	73	($3,030.23)	(3.05%)
	Sell	11/11/02	Sell	$1,319.19		($3,030.23)	$112,544.01	
11	Buy	11/21/02	Daily Breadth	$1,467.55	$0.00	68	($2,529.60)	(2.53%)
	Sell	12/04/02	Sell	$1,430.35		($2,529.60)	$110,014.41	
12	Buy	05/02/03	Daily Breadth	$1,502.88	$0.00	66	$7,119.42	7.18%
	Sell	06/23/03	Sell	$1,610.75		$7,119.42	$117,133.83	
13	Buy	08/29/03	Daily Breadth	$1,810.45	$0.00	55	$373.45	0.38%
	Sell	09/25/03	Sell	$1,817.24		$373.45	$117,507.28	
14	Buy	01/12/04	Daily Breadth	$2,111.78	$0.00	47	($1,617.27)	(1.63%)
	Sell	01/28/04	Sell	$2,077.37		($1,617.27)	$115,890.01	
15	Buy	04/05/04	Daily Breadth	$2,079.11	$0.00	48	($3,693.12)	(3.70%)
	Sell	04/15/04	Sell	$2,002.17		($3,693.12)	$112,196.89	
16	Buy	05/19/05	Daily Breadth	$2,042.58	$0.00	48	$513.12	0.52%
	Sell	06/24/05	Sell	$2,053.27		$513.12	$112,710.01	
17	Buy	08/30/06	Daily Breadth	$2,185.73	$0.00	45	$10,355.40	10.53%
	Sell	12/21/06	Sell	$2,415.85		$10,355.40	$123,065.41	
18	Buy	09/04/07	Daily Breadth	$2,630.24	$0.00	38	$3,606.96	3.61%
	Sell	10/19/07	Sell	$2,725.16		$3,606.96	$126,672.37	

While the 41% gain was certainly an outlier, half of the 12 winners achieved gains of greater than 10%, and the largest loser was less than 5%. Even in the low volatility environment of 2006 we see a 10% gain. So while more instances would certainly be preferable, it appears we have a decent amount of evidence here to suggest an upside edge.

The Nasdaq has now moved through its 50-day moving average and the S&P in on the verge of doing so. Support for the S&P around 800 held last week and there has been a lengthy consolidation from the November lows. With the Nasdaq attempting to take on a leadership position it is possible a rally could develop here. While I'm still not optimistic about the long-term picture a decent intermediate-term rally lasting a few months convincing some participants the worst may be behind us is already overdue. Intermediate-term traders may want to be at the ready to see if they can catch a multi-month move here soon. Should a rally emerge though it should be treated with great skepticism as it appears unlikely that it will be the beginning of a multi-year bull run. Selloffs may remain treacherous and traders may need to be nimble to avoid giving back rally gains.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Triggers

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	1.37
DJ US Regional Banks	IAT	3.75	DJ US Financial Services	IYG	2.80
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	0.50
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 significant capitulative action evident.

Additional New Trade Ideas

None tonight – I'm not seeing anything I love. There are some triggers listed on the "Systems Triggers" page on the website that more aggressive traders may look to exploit.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
IEF	2/5/2009	$93.90	$94.61	0.76%		sold on close
SPY(s)(1/4)	2/6/2009	$86.98	$83.11	4.66%		covered on close
SPY(s)(1/4)	2/9/2009	$87.10	$83.11	4.80%		
QQQQ(s)	2/9/2009	$31.39	$30.34	3.46%		covered on close

We just about had a decent month on Tuesday. Hopefully many of you were able to take advantage of the selling to some degree. If not, don't worry about it. There are typically 2-4 decent opportunities per month. It likely won't be long until the market sets up again in a favorable configuration.

Currently I am looking to exit the remaining SPY under following conditions.

At the open if it opens @ $82.70 or below.

On a close of $83.10 or lower.

I am not interested in trying to cover by chasing if the market gaps higher in the morning. Should a gap higher lead to an intraday selloff I will likely look to trail a stop as the day goes on. I may also put a stop on tomorrow if SPY gaps higher and then consolidates sideways for a period of time.