QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 31, 2009 Volume 2 Issue 61

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					
March 31, 2009	2 Down in Chop	1-3 days	Bullish		
March 31, 2009	Double Dn 1.75% No 10-low	1-7 days	Bullish	5.00%	7.90%
March 30, 2009	20 low range and vol while SPY>10ma	1-10 days	Bearish	-4.40%	-9.90%
March 25, 2009	20day high with low volume & range	1-10 days	Bearish	-2.50%	-4.60%
Active - Long Term					
March 26, 2009	Rise after follow through day		Bullish		
Dropped Tonight					
March 19, 2009	Appel Daily Breadth	1-20 days	Bullish		
March 20, 2009	Nas Spyx < 0 whil Nas > 10ma	1-7 days	Bearish	-5.10%	-10.90%
March 30, 2009	***Last Friday of Month drops > 1%***	***1 day***	***Bearish***	***-2.00%***	***-4.00%***
March 19, 2009	Fed Day Spike	1-8 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 3/31 – slightly bullish

Friday's weakness carried through to Monday as often happens. After gapping down over 2% the S&P 500 continued lower and finished the day down 3.5%. Breadth was extremely negative as NYSE Up Issues % came in at 11% and the Up Volume % was 5%. NYSE volume was low but still a little above Friday's levels.

Back in the July 29, 2008 blog and Subscriber Letter I looked a few different ways at instances where the S&P sold off 1.75% or more on 2 of 3 days. I found they generally had a positive expectation going forward – especially when the selling didn't result in a new 10-day low. Below is an updated table that looks at this scenario.

S&P 500 drops 1.75% or more today and either yesterday or the day before. Today's low is above the 10-day low. Buy on close. Sell X days later. $100k/trade. 1960-present.

Days In	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
10	$29,751.61	17	13	4	76.47	$4,265.11	($6,423.72)	0.66	2.16	$1,750.09
9	$42,582.21	17	13	4	76.47	$4,955.91	($5,461.17)	0.91	2.95	$2,504.84
8	$38,570.06	17	12	5	70.59	$4,581.09	($3,280.61)	1.40	3.35	$2,268.83
7	$47,333.20	19	14	5	73.68	$4,361.30	($2,745.01)	1.59	4.45	$2,491.22
6	$28,824.78	19	13	6	68.42	$3,905.86	($3,658.56)	1.07	2.31	$1,517.09
5	$23,842.66	19	14	5	73.68	$3,207.97	($4,213.79)	0.76	2.13	$1,254.88
4	$12,228.37	20	13	7	65.00	$3,446.32	($4,653.41)	0.74	1.38	$611.42
3	$1,200.25	20	14	6	70.00	$2,176.26	($4,877.90)	0.45	1.04	$60.01
2	$2,615.70	20	11	9	55.00	$1,818.08	($1,931.46)	0.94	1.15	$130.79
1	$1,000.66	23	15	8	65.22	$1,411.35	($2,521.19)	0.56	1.05	$43.51

Narrowing the field a little bit and requiring the S&P not even make a 7-day low, rather than a 10 provided the following results:

S&P 500 drops 1.75% or more today and either yesterday or the day before. Today's low is above the 7-day low.										
Buy on close. Sell X days later. $100k/trade. 1960-present.										
Days In	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
10	$35,818.82	12	10	2	83.33	$4,241.60	($3,298.59)	1.29	6.43	$2,984.90
9	$53,525.37	12	11	1	91.67	$4,922.32	($620.16)	7.94	87.31	$4,460.45
8	$44,165.20	12	10	2	83.33	$4,606.98	($952.29)	4.84	24.19	$3,680.43
7	$43,348.06	13	10	3	76.92	$4,541.61	($689.36)	6.59	21.96	$3,334.47
6	$38,656.13	13	11	2	84.62	$4,031.84	($2,847.04)	1.42	7.79	$2,973.55
5	$27,068.19	13	11	2	84.62	$3,660.48	($6,598.54)	0.55	3.05	$2,082.17
4	$18,115.60	14	10	4	71.43	$3,878.56	($5,167.49)	0.75	1.88	$1,293.97
3	$1,211.45	14	10	4	71.43	$2,448.08	($5,817.34)	0.42	1.05	$86.53
2	($30.26)	14	7	7	50.00	$1,797.79	($1,802.12)	1.00	1.00	($2.16)
1	($244.69)	15	9	6	60.00	$1,316.11	($2,014.94)	0.65	0.98	($16.31)

A bit too few instances for my taste. Overall though, these studies seem to suggest a bounce is likely.

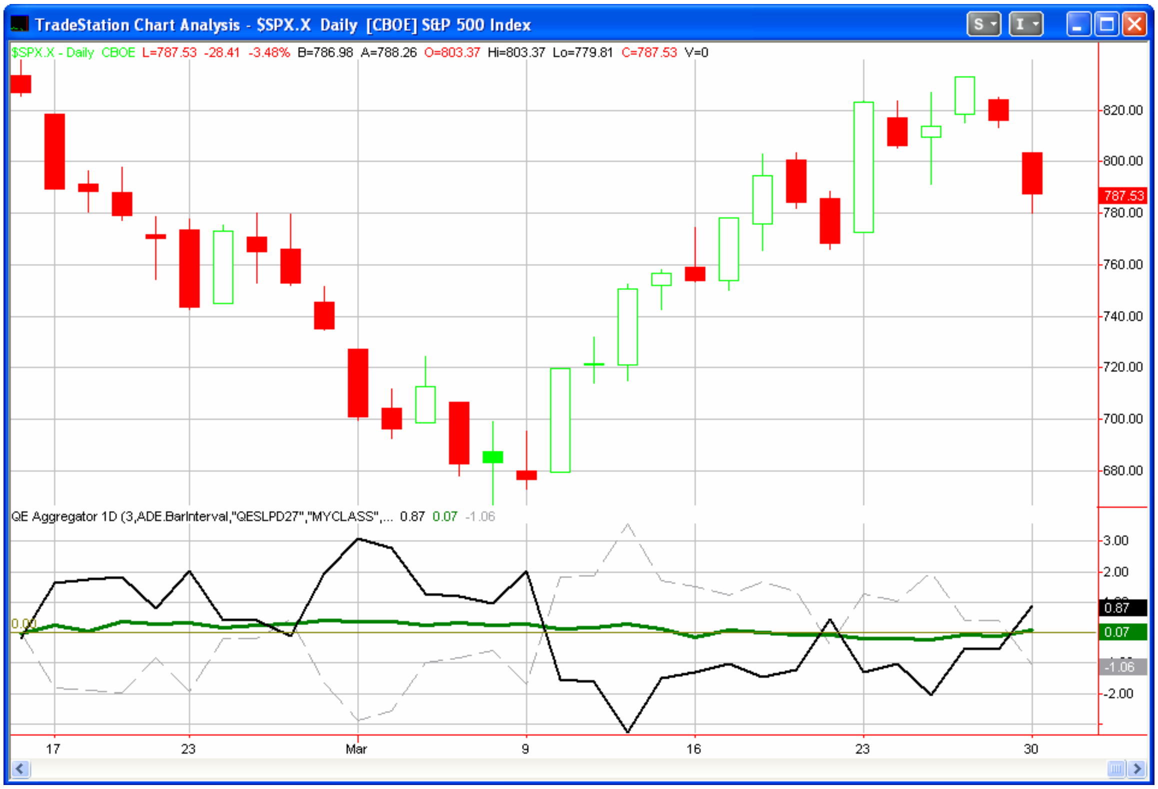
Also triggering today was our "2 Days Down In Chop" system. As a reminder this simple system buy the market at the close of the 2nd dwon day in a row. It then sells the 1s t close that would be a gain – up to 3 days later. After 3 days the position is exited regardless of profitability. Below is an updated results scorecard for the system:

TradeStation Performance Summary Collapse

All Trades

Total Net Profit	$39,399.00	Profit Factor	2.18
Gross Profit	$72,698.86	Gross Loss	($33,299.86)
Roll Over Credit	$0.00		
Open Position Profit/Loss	$0.00		
Select Total Net Profit	$28,682.97	Select Profit Factor	1.86
Select Gross Profit	$61,982.83	Select Gross Loss	($33,299.86)
Adjusted Total Net Profit	$17,021.50	Adjusted Profit Factor	1.38
Adjusted Gross Profit	$62,094.64	Adjusted Gross Loss	($45,073.14)
Total Number of Trades	55	Percent Profitable	85.45%
Winning Trades	47	Losing Trades	8
Even Trades	0		
Avg. Trade Net Profit	$716.35	Ratio Avg. Win:Avg. Loss	0.37
Avg. Winning Trade	$1,546.78	Avg. Losing Trade	($4,162.48)
Largest Winning Trade	$10,716.03	Largest Losing Trade	($10,506.45)
Largest Winner as % of Gross Profit	14.74%	Largest Loser as % of Gross Loss	31.55%

With the above studies considered tonight's Aggregator chart is below:



With tonight's short-term bullish studies the Aggregator has flipped to mildly positive. Meanwhile, Monday's strong selloff swung the black differential line to solidly positive. With both lines north of zero the Aggregator chart is in a buying formation. That is what I intend to do.

Intermediate-term Outlook (2 weeks – 2 months)–neutral -updated 3/30

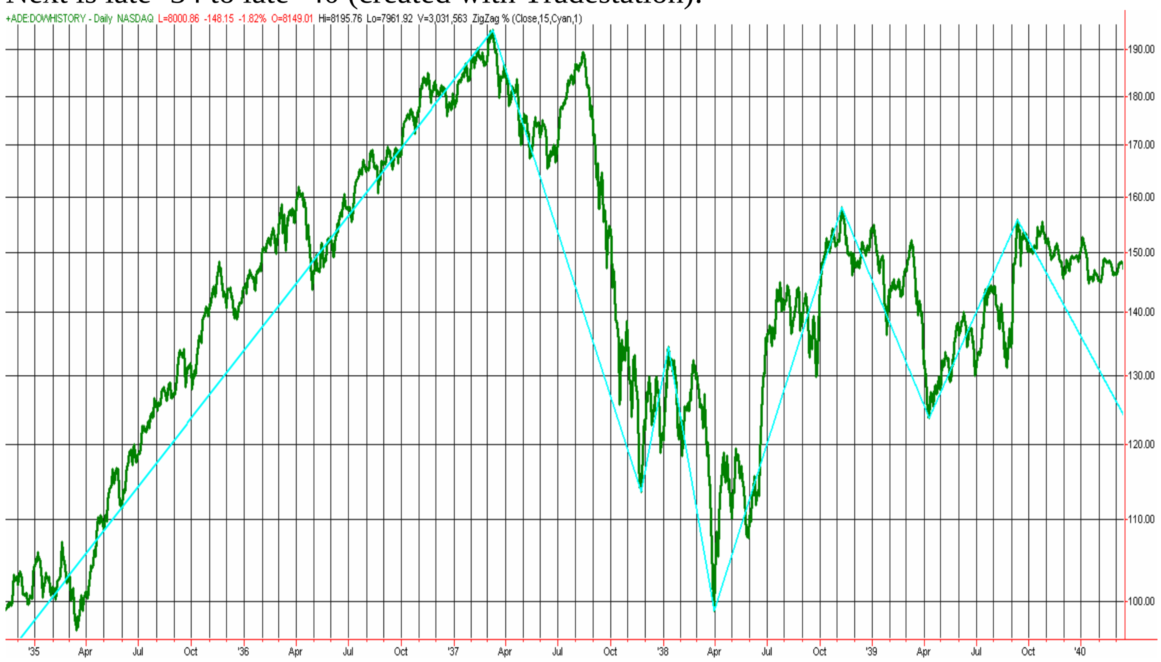
The question that I keep hearing over and over is "Is this rally for real?" What needs to be considered when formulating an answer is what constitutes a "real" bull move. It is my contention that the current environment most resembles that of the 30's from a trading standpoint. Certainly the kind of damage that has been done to the market has not occurred since at least that time period. Additionally, volatility levels reached during the course of this bear have reached levels not seen since at least the 30's in some cases.

I'm of the belief that the market is likely to trade in a very wide range over the next few years. It is unlikely to begin a new secular bull market during this time. Rather I believe we are likely to see both bull and bear runs occur. Some of these, such as the October and November rallies, may be too quick for most traders to capture significant portions of. Others may last several months before reversing course in a convincing manner. Below I've again pulled up some charts from the 30's. In this case I've overlayed the zig-zag indicator in light blue.

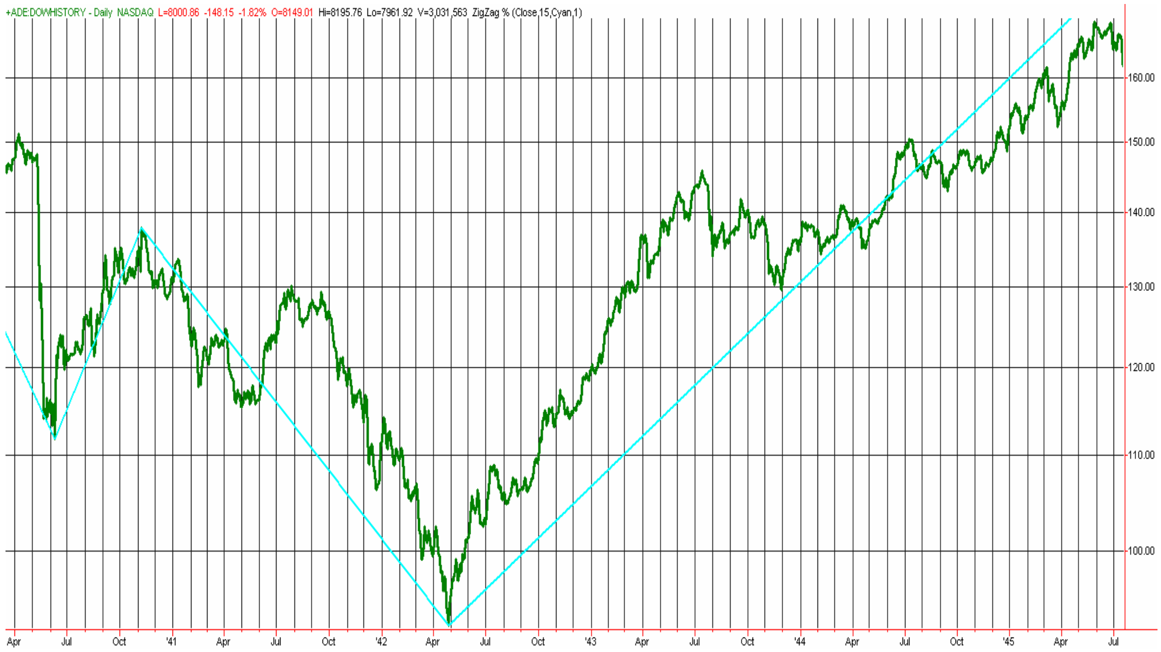
What the zig-zag does is identify all moves of at least 15% either up or down from close to close. You'll notice there was a substantial number of these moves during that time:

Late 1929 – late 1934. (created with Tradestation)

Next is late ’34 to late ’40 (created with Tradestation):



Several bull and bear markets could also be identified here. The next great bull move, though didn’t take place until 1942 as can be seen below:



So is it for real? Well, I'm not at all convinced that we're looking at a 1942 bottom at this point. My contention is we are likely years away from that. The moves seen between 1929 and 1941 offered plenty of opportunity, though. I expect the next several years of this market will as well. Traders need not worry whether we are in a bull or bear market. Leave that to the media and instead just focus on the likely direction based on the evidence for the next few days or weeks. Remain nimble in your assessment as conditions may change rapidly. Whether the "ultimate" bottom gets hit is irrelevant. The ultimate bottom in the charts above was made in 1932. Close to 10 years passed before the next great bull market emerged. Picking that 1932 ultimate bottom and riding the wave higher was not the key to big profits. Much more important than picking the bottom would have been to stay nimble and take advantage of some of the vast directional opportunities over the next 10 years – prior to the "real" bull emerging.

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	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	0.70
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	0.00
DJ US Consumer Svcs	IYC	0.00		Nasdaq 100	QQQQ	0.00

Nothing happening here.

Additional New Trade Ideas

SPY – buy ¼ index position @ $78.30 limit. I'm looking to buy on any further weakness Tuesday. The limit price is between Monday's low and closing prices.

Active Trades Table

Symbol	**Entry Date**	**Entry Price**	**Current Price**	**% Gain/Loss**	**Stop**	**Notes**
KO(s)	3/26/2009	$44.85	$43.92	2.07%		covered on close
SPY(1/4)(s)	3/26/2009	$83.11	$80.71	2.89%		avg exit price

I was a bit hasty in taking the profits on the SPY position. That said, nearly 3% on a countertrend index trade is something I'll be happy with every time.

KO was also covered at the close for a decent profit. The dollar amount gained per share on KO was just under $1. I'd mentioned that KO QX was a possible deep in the money front month call that could be used as a substitute for KO. (Please see Friday's Letter for more discussion on this, or click the options label on the blog for some posts that argue the pros and cons of using options to short-term trade.) On Friday morning I picked up some KO QX in order to track the how the possible options trade might line up against the stock. On Friday I purchased the KO QX put option for $7.60. I sold it a few minutes before the close Monday for $8.60 – making a full dollar per share on the transaction. This was an odd example because the option purchase actually worked out better than a stock short would have. This was primarily due to some lucky timing as I just happened to catch the right side of the wiggle. Most often I'll be giving up $0.10 to $0.20 to utilize the option instead of the stock. Two of the big advantages to the options are the lower capital outlay and the natural stop. Losing $0.10 or so in profits I view as the cost of closely managing risk.