QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 9, 2009 Volume 2 Issue 130

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 + 1/2 Std Dev
Active					
July 9, 2009	2 Days Down In Chop	1-3 days	Bullish		
7/8/2009 (also 7/6/09)	SPX 1% drop. Advance twice decliners	1-9 days	Bullish	2.80%	4.00%
July 8, 2009	Gap dn. Close 20lo. Opn top cls bottom.	1-2 days	Bullish	1.80%	2.50%
July 7, 2009	Weak breadth on up day	1-4 days	Bearish	-4.10%	-5.60%
July 7, 2009	***Weak bounce after 1.75% drop***	***1-3 days***	***Bearish***	***-2.20%***	***-3.00%***
June 29, 2009	***Low range and vol above 10ma***	***1-15 days***	***Bearish***	***-4.40%***	***-6.90%***
Active - Long Term					
June 26, 2009	VIX:VXV drops below 0.9	2-5 months	Bearish		
June 22, 2009	***VIX:VXV hits 100-day low***	***1-20 days***	***Bearish***	***-3.80%***	***-5.50%***
June 11, 2009	4-day tight range above 10ma	1-20 days	Bullish	4.00%	4.80%
June 10, 2009	Nasdaq/NYSE Volume High	1-20 days	Bearish		
June 1, 2009	Nasdaq Relative Strength Leading		Bullish		
Dropped Tonight					
July 6, 2009	SPY 1% gap. Open top/close bottom 12%	1-3 days	Bullish	5.30%	6.50%
June 26, 2009	***2 Days 7:3 up issues - no 10 high***	***1-8 days***	***Bearish***	***-4.30%***	***-5.90%***

If the avg max move is achieved the study will appear in **bold and brown**. If the avg + 1/2 std deviation is achieved, it will appear in ***bold italic blue*** and no longer be active.

Short-term Outlook (1-5 days) – updated 7/8 – neutral to slightly bearish

The highly anticipated breakdown in the S&P happened today. It didn't stick, though. After crashing through all major support levels the market managed to bounce anyway. The end result was basically a flat day. The Dow and Nasdaq closed up marginally and the S&P closed down marginally. Breadth was weak – even on the Nasdaq which closed up slightly. The NYSE Up Issues % came in at 36% and the Up Volume % at 30%. Total volume came in at the highest level in the last 7 days.

The one bearish study that showed up on the Quantifinder tonight was the one related to the poor Nasdaq breadth from the 4/24/09 nightly letter. I've updated that study below:

First let's look at how the Nasdaq has performed after it finished higher on bad breadth:

Nasdaq Up Issues % closes < 40%. Nasdaq closes higher. Buy Nasdaq on close. Sell X days later. $100k/trade. 2001-present.										
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	-38,106.70	10	5	5	50.00	1,686.21	-9,307.55	0.18	0.18	-3,810.67
9	-46,932.53	10	3	7	30.00	3,207.99	-8,079.50	0.40	0.17	-4,693.25
8	-43,372.80	10	4	6	40.00	2,034.11	-8,584.87	0.24	0.16	-4,337.28
7	-23,348.70	10	6	4	60.00	1,677.76	-8,353.82	0.20	0.30	-2,334.87
6	-20,346.96	10	4	6	40.00	1,807.46	-4,596.13	0.39	0.26	-2,034.70
5	-18,772.94	10	5	5	50.00	1,293.98	-5,048.56	0.26	0.26	-1,877.29
4	-15,698.20	10	5	5	50.00	1,567.96	-4,707.60	0.33	0.33	-1,569.82
3	-14,627.93	10	6	4	60.00	986.86	-5,137.28	0.19	0.29	-1,462.79
2	-2,944.45	11	8	3	72.73	993.10	-3,629.75	0.27	0.73	-267.68
1	-1,594.41	11	7	4	63.64	996.18	-2,141.93	0.47	0.81	-144.95

I also once again looked at S&P performance following such occurrences:

Nasdaq Up Issues % closes < 40%. Nasdaq closes higher. Buy SPX on close. Sell X days later. $100k/trade. 2001-present.										
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	-15,761.02	10	6	4	60.00	2,604.84	-7,847.51	0.33	0.50	-1,576.10
9	-24,440.87	10	3	7	30.00	4,153.09	-5,271.45	0.79	0.34	-2,444.09
8	-26,027.95	10	4	6	40.00	2,592.56	-6,066.36	0.43	0.28	-2,602.80
7	-13,270.15	10	6	4	60.00	2,279.11	-6,736.21	0.34	0.51	-1,327.02
6	-12,631.84	10	6	4	60.00	1,894.89	-6,000.30	0.32	0.47	-1,263.18
5	-9,566.73	10	6	4	60.00	1,570.40	-4,747.29	0.33	0.50	-956.67
4	-8,727.50	10	6	4	60.00	1,506.04	-4,440.94	0.34	0.51	-872.75
3	-11,101.10	10	5	5	50.00	1,696.46	-3,916.68	0.43	0.43	-1,110.11
2	-944.26	11	6	5	54.55	1,497.43	-1,985.76	0.75	0.90	-85.84
1	-1,264.43	11	6	5	54.55	1,161.66	-1,646.88	0.71	0.85	-114.95

Most notable in both cases are the magnitude of the losses. There have been some sharp selloffs following days like Wednesday. With such a small sample size I don't find the overall numbers compelling enough to include this study in the Aggregator tonight.

As many subscribers are well aware, Wednesday also triggered the oft-talked about "2 Days Down in Chop" strategy. Below are updated stats with regard to this strategy:

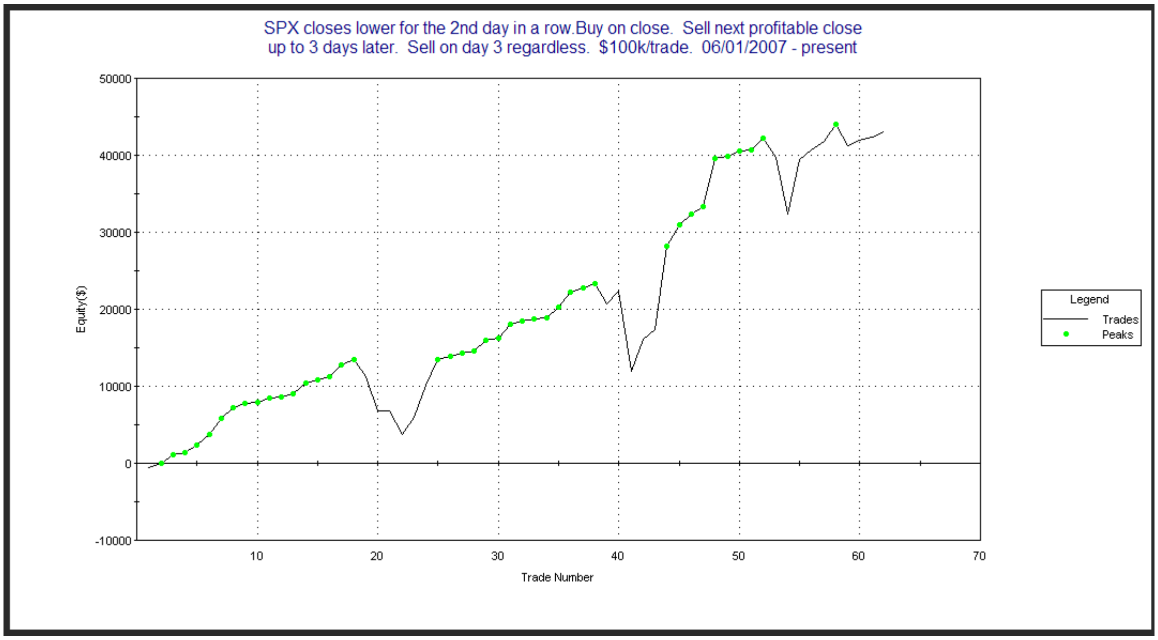
SPX closes lower for the 2nd day in a row.
Buy on close. Sell next profitable close up to 3 days later.
Sell on day 3 regardless. $100k/trade. 06/01/2007 - present

TradeStation Performance Summary — Collapse

All Trades

Total Net Profit	$43,017.18	Profit Factor	2.19
Gross Profit	$79,118.74	Gross Loss	($36,101.56)
Total Number of Trades	62	Percent Profitable	85.48%
Winning Trades	53	Losing Trades	9
Even Trades	0		
Avg. Trade Net Profit	$693.83	Ratio Avg. Win:Avg. Loss	0.37
Avg. Winning Trade	$1,492.81	Avg. Losing Trade	($4,011.28)
Largest Winning Trade	$10,716.03	Largest Losing Trade	($10,506.45)

I've also included a performance chart to go along with it:



In today's intraday update I discussed the VIX:VXV ratio trade idea that triggered a little over a week ago. I mentioned that using an alternate exit of a VIX stretch in addition to the standard "VIX:VXV closes above 1" exit enhanced returns. Time in the market was less and the total return was greater.

For those that would like to review this unofficial trade idea, you may use the link below:

2009-06-26 QE Subscriber Letter.pdf

Tonight I also tested how an SPX short would've performed historically based on my numbers and assumptions. First the basic strategy:

VIX:VXV Ratio drops below 0.9. Short SPX on close. Cover when VIX:VXV ratio closes >1. $100k/trade. 2002 - present.

TradeStation Performance Summary Collapse

All Trades			
Total Net Profit	$25,318.38	Profit Factor	2.37
Gross Profit	$43,784.97	Gross Loss	($18,466.59)
Total Number of Trades	15	Percent Profitable	73.33%
Winning Trades	11	Losing Trades	4
Even Trades	0		
Avg. Trade Net Profit	$1,687.89	Ratio Avg. Win:Avg. Loss	0.86
Avg. Winning Trade	$3,980.45	Avg. Losing Trade	($4,616.65)
Largest Winning Trade	$8,774.18	Largest Losing Trade	($7,985.67)
Largest Winner as % of Gross Profit	20.04%	Largest Loser as % of Gross Loss	43.24%
Max. Consecutive Winning Trades	5	Max. Consecutive Losing Trades	1
Avg. Bars in Winning Trades	38.45	Avg. Bars in Losing Trades	89.00
Avg. Bars in Total Trades	51.93		
Time in the Market	3 Yrs, 18 Dys	Longest Flat Period	289 Dys

Now a look at the performance when using the alternate exit technique:

VIX:VXV Ratio drops below 0.9. Short SPX on close. Cover when either 1) VIX:VXV ratio closes >1 or 2) VIX closes 15% above 10% envelope of 10ma. $100k/trade. 2002 - present.

All Trades			
Total Net Profit	$26,232.86	Profit Factor	2.90
Gross Profit	$40,052.85	Gross Loss	($13,819.99)
Total Number of Trades	20	Percent Profitable	70.00%
Winning Trades	14	Losing Trades	6
Even Trades	0		
Avg. Trade Net Profit	$1,311.64	Ratio Avg. Win:Avg. Loss	1.24
Avg. Winning Trade	$2,860.92	Avg. Losing Trade	($2,303.33)
Largest Winning Trade	$6,660.72	Largest Losing Trade	($6,662.81)
Largest Winner as % of Gross Profit	16.63%	Largest Loser as % of Gross Loss	48.21%
Max. Consecutive Winning Trades	5	Max. Consecutive Losing Trades	2
Avg. Bars in Winning Trades	29.14	Avg. Bars in Losing Trades	44.00
Avg. Bars in Total Trades	33.60		
Time in the Market	2 Yrs, 7 Mths, 7 Dys	Longest Flat Period	294 Dys

Here again we see that time in the market is reduced. Profits are nearly identical.

And how did the VXX trade work out? Remember, while shorting the S&P is one way to play a very low VIX:VXV ratio, another way would be to buy the VXX, which should rise in a manner similar to the VIX. The purchase would have taken place on June 25th.

If closed out today, the VIX would have gained 18.7% while VXX gained just under 5%. I find the difference in magnitude to be quite disappointing.

I've updated the Aggregator chart below:

The green Aggregator line is now slightly above zero, indicating a mild positive net expectancy for the S&P over the next few days. Meanwhile the market has underperformed expectations by a decent amount the last few days as illustrated by the black Differential line. Oversold with positive expectations is the preferred configuration when considering long entries and this fits that description.

You'll notice on the active studies list at the top of the letter that a good number of bearish studies have now hit their lower target. I typically removed the studies after they reach their upper targets. A few are quite close at this point. It's a judgment call deciding when they've traded far enough based on average max moves. With so many on the cusp I may elect to remove a couple in the next few days.

I'm not crazy about getting too aggressive here since the market may be in the process of a larger breakdown. While I would have preferred to have closed near the low of the day, the fact that we held support and rebounded may give hope to the bulls and allow them to rally for a few days. I'll look to scale in if I can find a favorable entry tomorrow. I've laid out my entry criteria in the "Trade Ideas" section below. The recent breakdown and possible topping formation will have me looking to take profits quickly if they develop. I am now considering the trend to be down and will treat long trades as counter-trend.

Intermediate-term Outlook (2 weeks – 2 months)– updated 7/6 – neutral (near turning bearish)

I don't often get into pure chart analysis in the Letter, but I thought I'd point out some things I'm watching closely on the chart below.

We're looking at the S&P 500 and an important area on the chart is the one I've circled in green above. As you'll note, we're only a few points above this area at the moment. What is striking me about this area is that there are several levels of potential support. Many of these will be fairly obvious to most technical traders. The thin pink rising line near the top of the green circle represents the neckline of a potential head and shoulders topping pattern. Just below that around 888 is where you'll find the 200ma and the June 23rd swing low, both of which could act as support. The 2nd blue line around 879 coincides with the May lows which also would mark the low of the left shoulder.

I'm not pointing out anything here that isn't fairly obvious to many technical traders. In fact, I would venture to guess that most traders that use charts would be considering at least one of the above points on their chart as important. It may be the Head and Shoulders pattern, it may be the price support, or it may be the 200ma. Whatever they're looking at, there is sure to be a lot of people focusing on this one relatively small area on the chart. The more levels of potential support or resistance that exist in a small area the more important that area becomes. With so many traders focusing on a particular area, moves around that area can be especially sharp, especially if the potential support breaks.

The intermediate-term studies are somewhat mixed at this point. I'm seeing bearish indications from sentiment indicators such as the Nasdaq/NYSE volume ratio and the VIX:VXV ratio. Meanwhile the Nasdaq/S&P lead/lag model still shows the Nasdaq as the current leader, which favors the bullish case. Also, while close to breaking down and possibly carving out a bearish Head and Shoulders pattern, the market has not yet violated any major support levels. I tend to give the primary trend the benefit of the doubt until it actually does change on a price chart.

With all this is mind I intend to tread a bit lightly until the market either bounces off this potential support level or slices through it. I'd rather not get caught on the wrong side of this action and I don't see a clear edge at this point. If I had to venture a guess, I'd guess the market is likely to retrace a bit more of the March – June rally. I think this support level will give way in the next few weeks. Whether this inclination turns out to be right or wrong will have little effect on my trading profits. I'll continue to re-evaluate on a daily basis. When the picture becomes more clear from an intermediate-term standpoint then I'll feel better about trading more aggressively on at least one side of the market.

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	0.73
DJ US Regional Banks	IAT	2.99		DJ US Financial Services	IYG	1.56
DJ US Utilities	IDU	0.00		DJ US Healthcare	IYH	0.74
DJ US Oil&Gas Expl & Prod	IEO	1.64		DJ US Industrial Sector	IYJ	1.52
DJ US Oil Equip & Svcs	IEZ	0.00		DJ US Consumer Goods	IYK	0.00
DJ US Pharmaceuticals	IHE	2.86		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	2.56		DJ US Transportation	IYT	5.00
DJ US Aerospace & Defense	ITA	2.94		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	1.00

While selling has picked up the last few days, the CBI %'s are not uncovering any substantial capitulative action.

Additional New Trade Ideas

A full listing of system triggers can be found at the system triggers page each night. I will cherry pick some of my favorite setups from the S&P 100 and ETF lists along with occasional other trade ideas to track below.

SPY – buy ¼ index position under ONE of the following conditions

1) *At $87.30 limit on OPEN*
2) *At $87.10 limit*
3) *At $87.90 limit on close*

Based on short-term market outlook.

Active Trades Table

None