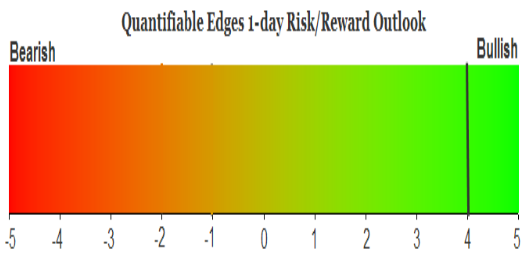
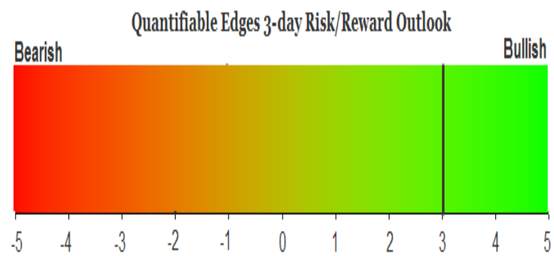
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 3, 2009 Volume 2 Issue 169

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
Active				
September 3, 2009	Big down then little down	1-6 days	Bullish	2.40%
September 3, 2009	2 down in chop	1-4 days	Bullish	2.70%
September 2, 2009	1% drop heavy vol no 10-low	1-5 days	Bearish	-2.90%
August 28, 2009	2 down in chop	1-3 days	Bullish	
August 28, 2009	False breakdown & close at new high	1-5 days	Bullish	2.00%
Active - Long Term				
July 14, 2009	VIX:VXV drops below 0.9	2-5 months	Bearish	
Dropped Tonight				
September 2, 2009	94% dowside volume. No 10-low	1 days	Bullish	

If the avg max move is achieved the study will appear in ***bold italic blue*** and no longer be active.

Short-term Outlook – updated 9/3

The Bottom Line

The market remains oversold and the studies remain bullish. It appears the odds strongly favor a bounce within the next few days. The studies tonight looked at early-month selloffs and sharp drops that lose some steam. All studies favored a bullish short-term outlook.

The Proof

After gapping down the market failed to bounce in a meaningful way on Wednesday. It traded in a relatively narrow range for most of the day. When it was over it closed above the open but still down on the day. Breadth was a bit negative with the NYSE Up Issues % at 38% and the Up Volume % at 41%. Total volume sank but was still above normal.

Beginning of months is a seasonally strong time. The market rises on most occasions. It is fairly rare to see a month start off with two down days. I last looked at bad starts to the month in the blog on June 4, 2008. I've updated that study below:

SPY closes down the 1st 2 days of the month and loses at least 1.5%.
Buy on close. Sell X days later. $100k.trade. 1994-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
5	19,390.16	16	11	5	68.75	2,481.59	-1,581.47	1.57	3.45	1,211.89
4	19,353.70	16	12	4	75.00	2,095.43	-1,447.85	1.45	4.34	1,209.61
3	15,290.38	16	10	6	62.50	2,078.91	-916.45	2.27	3.78	955.65
2	11,663.32	16	7	8	43.75	2,550.39	-773.68	3.30	2.88	728.96
1	2,752.75	16	10	6	62.50	867.78	-987.51	0.88	1.46	172.05

All 16 instances posted a close above the entry price at some point in the next week.

16 for 16 bouncing at some point in the next week suggests a pretty good chance we see a bounce here soon.

One theme among several of the studies identified by the Quantifinder today was that when a sharp selloff loses steam it often leads to a bounce. This was looked at a few different ways. The 2/19/09 Nightly Letter looked at days where small drops followed big ones.

After dropping over 1.75% yesterday the SPX falls less than 0.5% today.
Buy on close. Sell X days later. $100k/trade. 1988 - 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	40,703.08	35	23	12	65.71	3,362.84	-3,053.53	1.10	2.11	1,162.95
9	48,780.69	36	26	10	72.22	3,048.29	-3,047.48	1.00	2.60	1,355.02
8	51,252.01	36	24	12	66.67	3,331.79	-2,392.59	1.39	2.79	1,423.67
7	44,529.67	36	26	10	72.22	2,707.34	-2,586.11	1.05	2.72	1,236.94
6	42,933.38	36	23	13	63.89	2,687.46	-1,452.17	1.85	3.27	1,192.59
5	29,977.81	36	22	14	61.11	2,344.46	-1,542.88	1.52	2.39	832.72
4	23,459.51	37	23	14	62.16	2,277.35	-2,065.68	1.10	1.81	634.04
3	10,251.02	37	23	14	62.16	1,867.49	-2,335.80	0.80	1.31	277.05
2	4,846.53	37	21	16	56.76	1,405.85	-1,542.27	0.91	1.20	130.99
1	3,655.82	37	23	14	62.16	1,009.25	-1,396.93	0.72	1.19	98.81

32 of 37 (86.5%) instances closed above the entry price at some point in the next week.

Again we are looking at a high percentage bounce and a net positive expectation over the next several days. More detail on this study may be found in the 2/19/09 Letter, which can be found on the archives page.

You could also evaluate the 2-day pattern by looking wide range (WR7) and narrow range bars (NR7). I did this in the 6/24/08 subscriber Letter and blog. I've updated the Subscriber Letter study below:

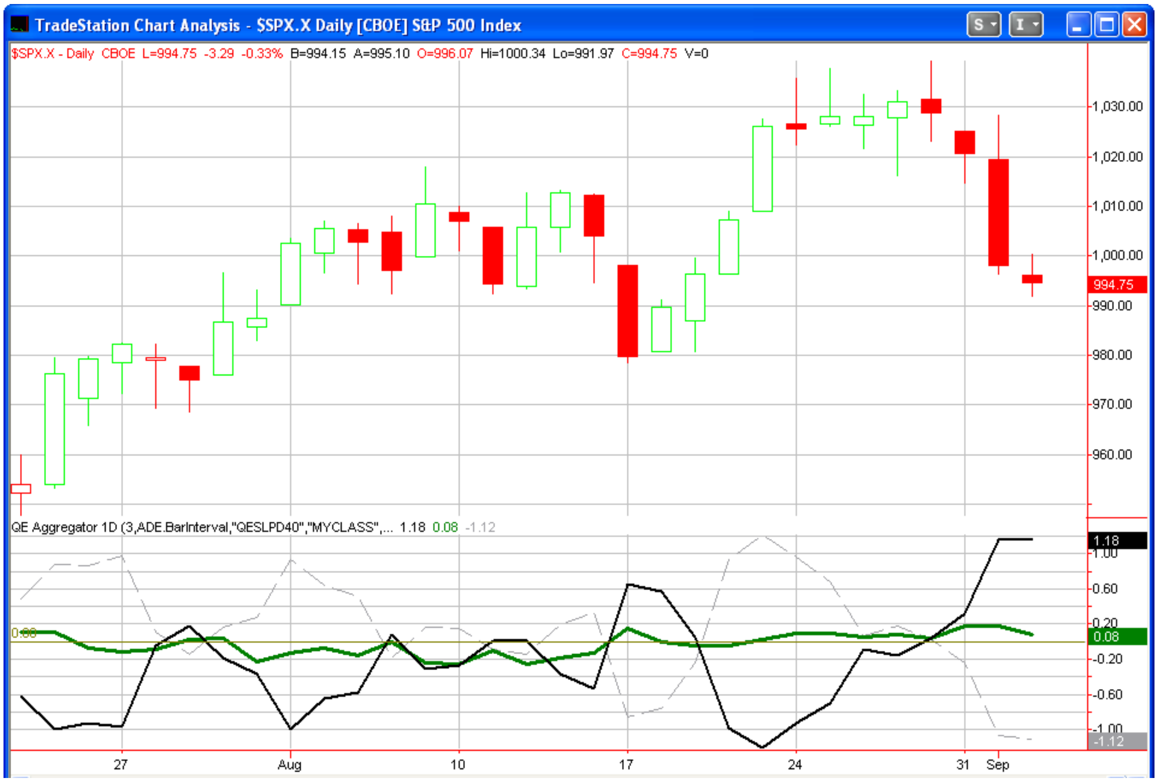
Yesterday SPX makes a WR7 down on the highest volume in 10 days. Today it posts an NR7. Buy on close. Sell X dyas later. $100k/trade. 1978 - present.

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	14,997.00	15	11	4	73.33	2,476.72	-3,061.73	0.81	2.22	999.80
9	19,764.10	15	11	4	73.33	2,615.76	-2,252.32	1.16	3.19	1,317.61
8	20,391.20	15	10	5	66.67	2,942.10	-1,805.96	1.63	3.26	1,359.41
7	15,877.51	15	9	6	60.00	2,829.93	-1,598.64	1.77	2.66	1,058.50
6	12,494.22	15	9	6	60.00	2,280.81	-1,338.85	1.70	2.56	832.95
5	13,599.00	15	12	3	80.00	1,651.35	-2,072.38	0.80	3.19	906.60
4	10,509.24	15	10	5	66.67	1,816.19	-1,530.53	1.19	2.37	700.62
3	1,237.16	15	9	6	60.00	1,293.02	-1,733.34	0.75	1.12	82.48
2	1,283.19	15	10	5	66.67	861.52	-1,466.40	0.59	1.18	85.55
1	89.90	15	8	7	53.33	839.07	-946.10	0.89	1.01	5.99

14 of 15 instances (93%) close above their entry price at some point in the next week. The lone holdout was 9/18/01, which took another 3 days before posting a profitable close.

Overall the deceleration in the selloff is suggesting a good chance the market will bounce shortly.

The Aggregator chart is updated below.



The configuration of the Aggregator chart hasn't changed much today. The green Aggregator line remains squarely above 0, indicating net positive expectations from the active studies over the next few days. The black differential line still shows the S&P has strongly underperformed expectations over the last 3 days. Strongly oversold with positive expectations typically provides a bullish edge.

I'll be looking to get long again tomorrow as discussed in the trade ideas section below. With the addition of the new bullish studies tonight it now appears much less likely that the Aggregator will flip to bearish without some kind of rally. This means I'll be keeping stops looser and giving the setup more of a chance to work than I have the last 2 days.

Intermediate-term Outlook (2 weeks – 2 months)– updated 8/31 – very slightly bullish

A week of going nowhere has done nothing to clarify the intermediate-term picture. Breadth was the big discussion in last week's outlook nothing was resolved there. The 90% up day on Friday the 21st has not been closely followed by another breadth surge. If it had that would have hinted at real strength.

I also discussed in detail how the number of stocks hitting new 52-week highs had shrunk since late July / early August. While the market was hitting new highs the stocks participating in those highs was declining. As I showed, this is not a death sentence for the rally. Results going forward were mixed. The market outlook does improve substantially, though, when the number of new highs is expanding and confirming the index highs.

The other indicators that have provided some interesting studies over the last several weeks haven't changed at all in the past week, either. Negative indications such as the low VIX:VXV ratio, the excessive Nasdaq vs. NYSE volume and the generally downsloping total volume over the last few months are still in play. Of course the negative effects of these indicators has been slow to kick in.

Right now the market is still in rally mode, and betting against it for any extended period of time has not worked. Short trades need to be small and profits taken when available. I expect we're going to see a substantial selloff begin at some point in the next 2-3 months. I don't see compelling evidence of it just yet.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Triggers

CAT – buy 1/3 position at $43.84 (bought @ $43.84)
CAT – buy 1/3 position @ $43.51

Catapult for ETF's Trades

IWN – buy @ $52.12

Also notable is that SPY is set up as a Catapult for ETF. It has done very well as a Catapult over the years. Below is a catapult performance report for SPY:

Catapult for ETF performance of SPY.
$100k/trade. 1994-present.

TradeStation Performance Summary — Collapse

All Trades

Total Net Profit	$72,169.79	Profit Factor	22.73
Gross Profit	$75,490.51	Gross Loss	($3,320.72)
Total Number of Trades	17	Percent Profitable	94.12%
Winning Trades	16	Losing Trades	1
Even Trades	0		
Avg. Trade Net Profit	$4,245.28	Ratio Avg. Win:Avg. Loss	1.42
Avg. Winning Trade	$4,718.16	Avg. Losing Trade	($3,320.72)
Largest Winning Trade	$12,275.00	Largest Losing Trade	($3,320.72)

Broad Market Large Cap CBI –2(CAT-2)

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 1/4 index position @ $99.90 limit and ¼ index position @ $99.25 limit. I'm looking to take a little larger size here than usual for 2 reasons 1) The Aggregator is no longer in danger of flipping to bearish as was the case last night, and 2) SPY is also setup as a Catapult for ETF trade.

CAT – 1/3 position based on Catapult trade above. This would be the 2nd lot of 1/3 position size. Remember that Catapults are capable of being very volatile trades and I typically trade them without stops. Keep this in mind when considering position size if you decide to trade it.

IWN – buy @ $52.12 limit. A Catapult for ETF trade as noted above. I don't always scale into the ETF versions of the Catapults. Like the stock Catapults, they are very volatile and traded primarily without a stop, so position sizing is paramount.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Pr	% Gain/Lo	Stop	Notes
SPY(1/4)	9/2/2009	$99.78	$99.60	-0.18%		stopped out intraday
CAT(1/3)	9/2/2009	$43.84	$43.51	-0.75%		

Unfortunately the intraday stop I placed today in SPY managed to pick the bottom. That's just part of trading sometimes.