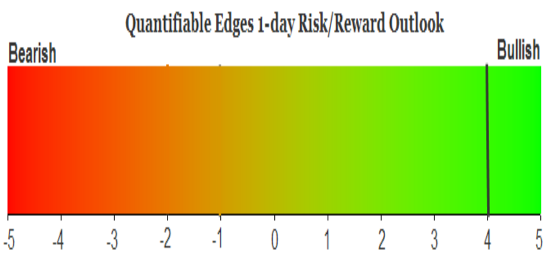
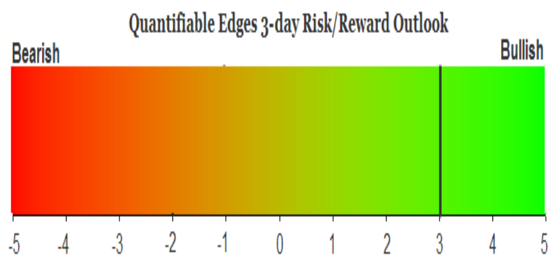
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 24, 2009 Volume 2 Issue 183

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 24, 2009	SPX down 1% SOX up	1-6 days	Bullish	
September 24, 2009	Fed Day Reversal to close poorly	1 day	Bullish	
September 21, 2009	Op-ex week up 2%-3%	1-5 days	Bearish	-1.20%
Active - Long Term				
September 14, 2009	Nasdaq/S&P Lead/Lag Model		Bullish	
September 11, 2009	Appel Daily Breadth Impulse Signal	1-20 days	Bullish	5.00%
July 14, 2009	VIX:VXV drops below 0.9	2-5 months	Bearish	
Dropped Tonight				
September 23, 2009	Fed Day	1 day	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 9/24

The Bottom Line

Despite a run of positive recent Fed days the market reversed hard after initially rallying Wednesday. The selloff looked ugly as the market plummeted late in the day. Tonight's studies are suggesting that such swoons are often reversed and we appear to have a bullish edge over the next few days.

The Evidence

The market spent the morning meandering about awaiting the Fed announcement. After the announcement it rallied sharply for a short while. Once 3pm arrived though the sellers arrived. The market fell steadily and strongly over the last hour. The S&P lost over 1% and the Nasdaq nearly ¾%. Breadth was decidedly negative. The NYSE Up Issues % was 35% and the Up Volume % just 19%. Total volume increased slightly but was still below average.

The generally positive bias of Fed days that I looked at last night didn't hold up today. The late selloff looks especially foreboding on a chart but the Quantifinder provided a few indications that today's action was actually short-term bullish.

One study that popped up today was originally from the 8/13/08 blog. It looked at times when the S&P has sold off 1% or more during the day but the semiconductor index (SOX) has closed higher. I updated the results below:

SPX drops more than 1% while SOX closes postiive on the day.
Buy SPX on close. Sell X days later. $100k/trade. 1995 - 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
20	91,591.22	35	29	6	82.86	3,938.10	-3,768.95	1.04	5.05	2,616.89
19	80,625.51	35	28	7	80.00	3,893.75	-4,057.09	0.96	3.84	2,303.59
18	79,862.72	36	28	8	77.78	4,007.52	-4,043.49	0.99	3.47	2,218.41
17	87,329.39	36	31	5	86.11	3,578.63	-4,721.62	0.76	4.70	2,425.82
16	90,998.96	36	30	6	83.33	3,608.40	-2,875.51	1.25	6.27	2,527.75
15	89,496.45	38	32	6	84.21	3,418.23	-3,314.51	1.03	5.50	2,355.17
14	82,469.93	38	29	9	76.32	3,510.81	-2,149.30	1.63	5.26	2,170.26
13	68,128.29	39	31	8	79.49	3,163.58	-3,742.83	0.85	3.28	1,746.88
12	55,304.42	39	30	9	76.92	2,773.84	-3,101.20	0.89	2.98	1,418.06
11	59,499.84	39	29	10	74.36	3,259.40	-3,502.27	0.93	2.70	1,525.64
10	40,218.70	39	29	10	74.36	2,668.81	-3,717.69	0.72	2.08	1,031.25
9	34,405.79	41	28	13	68.29	2,571.61	-2,892.25	0.89	1.92	839.17
8	48,546.57	41	28	13	68.29	2,680.37	-2,038.75	1.31	2.83	1,184.06
7	53,549.57	42	29	13	69.05	2,808.18	-2,145.21	1.31	2.92	1,274.99
6	53,557.93	43	32	11	74.42	2,744.65	-3,115.52	0.88	2.56	1,245.53
5	44,549.88	44	29	15	65.91	2,693.81	-2,238.05	1.20	2.33	1,012.50
4	40,465.18	44	28	16	63.64	2,369.19	-1,617.01	1.47	2.56	919.66
3	24,069.86	46	27	19	58.70	2,231.22	-1,903.84	1.17	1.67	523.26
2	19,152.78	47	26	21	55.32	2,010.52	-1,577.18	1.27	1.58	407.51
1	16,006.30	49	23	26	46.94	1,611.25	-809.71	1.99	1.76	326.66

87% of instances closed higher than the entry price at some point in the next week.

The positive inclinations here have often played out well beyond the initial 5-6 days.

I've also looked at reversals from highs and reversals on Fed days before – both in the May 1, 2008 blog. I also re-ran those studies below:

SPX makes 20-day intraday high and close in the bottom 10% of daily range.
Buy on close. Hold X days. $100k/trade. 1980 - 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	53,199.37	79	49	30	62.03	2,081.21	-1,626.00	1.28	2.09	673.41
9	36,454.92	80	46	34	57.50	1,938.34	-1,550.26	1.25	1.69	455.69
8	44,133.60	82	53	29	64.63	1,753.40	-1,682.64	1.04	1.90	538.21
7	38,879.29	82	53	29	64.63	1,641.83	-1,659.92	0.99	1.81	474.14
6	28,802.27	84	53	31	63.10	1,440.29	-1,533.33	0.94	1.61	342.88
5	16,110.50	86	48	38	55.81	1,337.98	-1,266.12	1.06	1.33	187.33
4	12,518.20	88	46	42	52.27	1,309.32	-1,135.96	1.15	1.26	142.25
3	18,645.27	88	50	38	56.82	1,104.39	-962.47	1.15	1.51	211.88
2	9,252.41	88	45	43	51.14	935.10	-763.42	1.22	1.28	105.14
1	14,351.56	89	52	37	58.43	649.21	-524.52	1.24	1.74	161.25

There appears to be an upside edge here. Although it isn't the most powerful edge we've seen it still appears to suggest bullish inclinations over the next few days and weeks.

Also in that May 1, 2008 blog I looked specifically at Fed days that closed in the bottom 10% of their daily range. I re-ran that study as well tonight.

SPX closes in bottom 10% of daily range on a Fed day. Buy on close. Sell X
days later.$100k/trade. 1982 - 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	26,571.38	33	20	13	60.61	3,068.24	-2,676.42	1.15	1.76	805.19
9	28,479.23	33	26	7	78.79	2,441.11	-4,998.51	0.49	1.81	863.01
8	15,422.57	33	23	10	69.70	2,400.77	-3,979.51	0.60	1.39	467.35
7	8,151.78	33	20	13	60.61	2,488.19	-3,200.93	0.78	1.20	247.02
6	3,246.98	34	20	14	58.82	2,398.97	-3,195.18	0.75	1.07	95.50
5	14,626.23	34	21	13	61.76	2,052.26	-2,190.09	0.94	1.51	430.18
4	16,401.90	34	20	14	58.82	1,926.81	-1,581.02	1.22	1.74	482.41
3	5,051.94	34	22	12	64.71	1,371.61	-2,093.63	0.66	1.20	148.59
2	8,556.53	34	20	14	58.82	1,585.37	-1,653.64	0.96	1.37	251.66
1	17,885.44	34	23	11	67.65	1,299.00	-1,090.15	1.19	2.49	526.04

Much of the edge here appears in the first day. Poor closes on Fed days have rarely seen significant follow through in the coming days. More often the selling is viewed as an overreaction and the market is able to rebound a bit.

I combined the fact that the market had a reversal from a new high with the fact that it was a fed day. The below study shows the results of the 6 times we've seen a 10-day high reverse hard and close lower on a Fed day.

On Fed Day SPX makes a 10-day high and then reverses to close over 1% below it's intraday high and down on the day. Buy on close. Sell next days close. $100k/trade. 1982-present.

Date/Time	Signal	Price	% Profit	Run-up DrawDown
08/24/82	Buy	$115.33	1.95%	$2,982.48
08/25/82	Sell	$117.58		($676.26)
10/05/99	Buy	$1,301.35	1.85%	$1,832.36
10/06/99	Sell	$1,325.40		$0.00
01/31/01	Buy	$1,366.01	0.54%	$543.12
02/01/01	Sell	$1,373.45		($486.91)
04/11/01	Buy	$1,166.46	1.46%	$1,449.25
04/12/01	Sell	$1,183.51		($742.05)
12/11/07	Buy	$1,477.62	0.61%	$2,300.78
12/12/07	Sell	$1,486.60		($629.13)
04/30/08	Buy	$1,385.58	1.71%	$1,763.28
05/01/08	Sell	$1,409.34		($180.72)

So here we have yet another test suggesting upside tomorrow.

One subscriber wrote me and was concerned that the poor finish seem out of character for the recent rally and that it could be an ominous sign. I decided to look at a ll other times the market has closed in the bottom 10% of its range since the March bottom. While it may seem like the market has been consistently closing strongly, this is the 16th day we've seen a close in the bottom 10% of the day's range. Below are some stats on the previous 15 times.

SPX closes in the bottom 10% of daily range. Buy on close. Hold X days. $100k/trade. 3/6/09 - present.

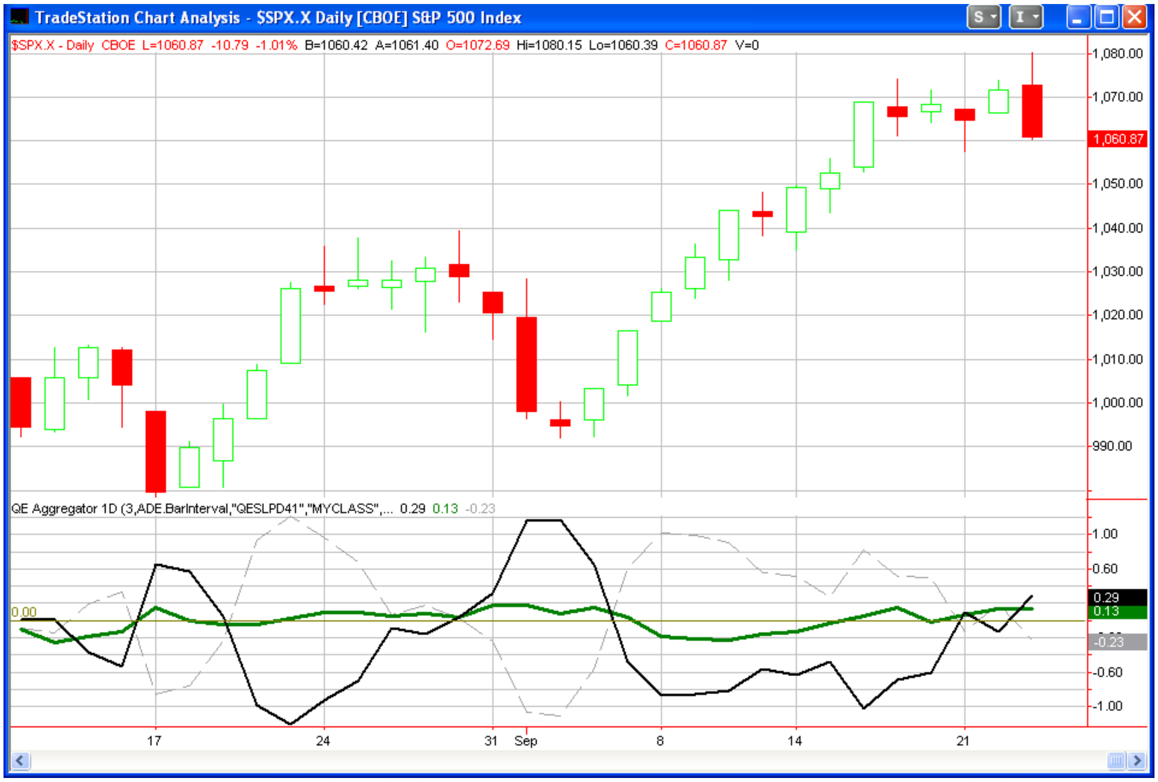
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
3	27,422.02	13	11	2	84.62	2,824.28	-1,822.55	1.55	8.52	2,109.39
2	18,253.82	15	11	4	73.33	2,242.03	-1,602.12	1.40	3.85	1,216.92
1	10,328.92	15	10	5	66.67	1,272.38	-478.97	2.66	5.31	688.59

Of the 15 instances only 1 (5/11/09) failed to close higher than the entryprice at some point in the next 3 days

Of the 15 instances only 1 (5/20/09) failed to trade above the closing price at some point the next day.

This doesn't tell us a whole lot since the study was run in a period of extreme bullishness. Still, with now 16 instances it would seem to be not such a rare occurrence. So far I see no reason to be concerned about Wednesday's selloff. When presented with all the other bullish evidence tonight we appear to have a pretty good case for a bounce.

The Aggregator chart is updated below.



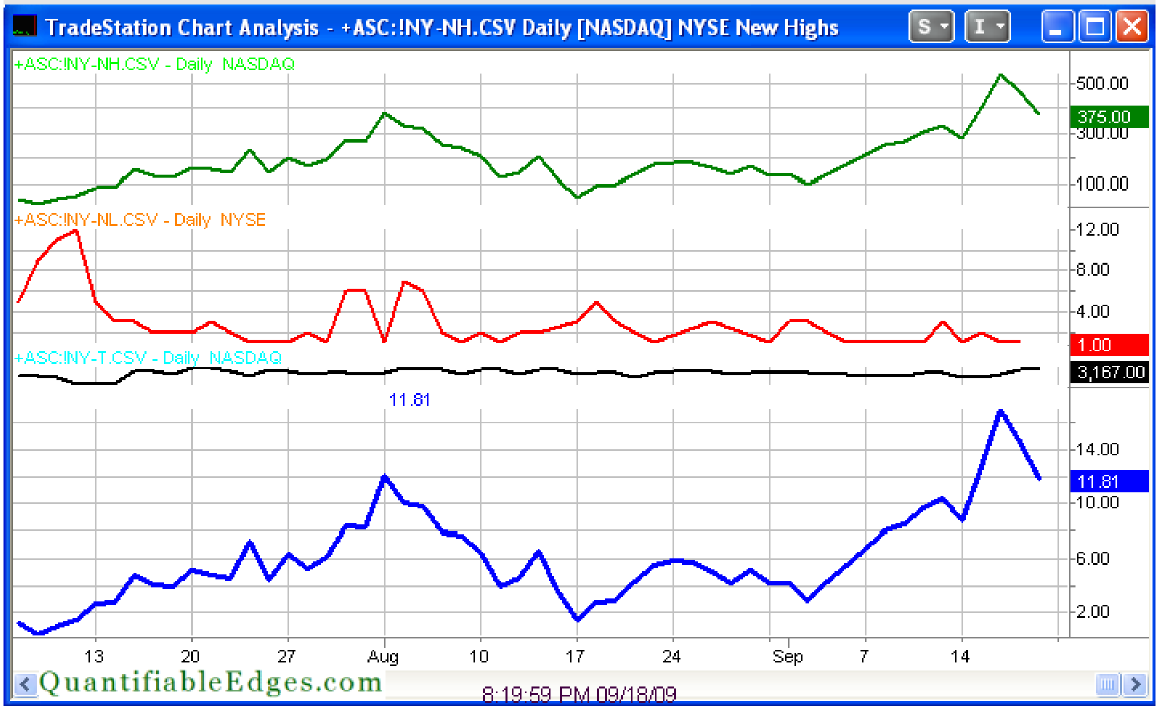
As noted was probable in the late-day update the Aggregator chart has a bullish configuration. The green Aggregator line is squarely above zero, illustrated the net positive expectations of the active studies. The black Differential line also flipped positive today as the SPX has now underperformed expectations over the last few days. Both lines above zero suggest a bullish edge over the next few days.

I'll be looking to take on some long exposure in the trade ideas section below.

Intermediate-term Outlook (2 weeks – 2 months)– updated 9/21 – somewhat bullish
Nothing really has changed since last week from an intermediate-term standpoint. In last week's Letter we reviewed 2 bullish indications and one bearish. The bullish indications came from 1) the Nasdaq/S&P 500 Relative strength chart, which is tracked on the website and 2) The Appel Daily Breadth Thrust signal which is triggered by a high reading in the Up Issues % 10-day ema. This can also be seen on the charts page. Both of these indicators remain bullish. We'll need to see continued outperformance by the Nasdaq and solid breadth readings this week for both indicators to remain bullish.

I also noted last week that it was worth keeping an eye on the NYSE Net New Highs %. It had failed to register a new high since August 1st, even while the indices had all been hitting new highs. My research showed that this was not a death sentence for the rally but that if the new highs could expand that would serve as confirmation for the rally. Under such circumstances the market has historically outperformed the times new highs weren't confirming. This week saw a large expansion of new highs and the August levels were easily taken out. Below is a copy of the chart kept on the website that illustrates this.

NYSE Net New Highs



The current lone dissenter among the intermediate-term studies was the low VIX:VXV ratio study. This ratio remains stretched to the downside and is still suggesting an uptick in volatility, which would likely be accompanied by a market selloff. Interestingly, while this ratio remains stretched the VIX and the VXO are both right around their 10-day moving averages.

My conclusion remains the same as last week:

As long as I see the Nasdaq lead, breadth remain strong, and the new highs continue to expand, I'll look for a continuation of the current rally. All of these indications can flip in a fairly short period so they will need to be monitored. At some point the market will likely undergo a sharp correction.

The basic premise I'm working under remains that we are in a 1930's – style environment in which both rallies and selloffs will be much more exaggerated than most market participants are used to. Just as the bear market up to March 2009 was incredibly extreme, so has been the rally since then. I believe there is going to be a lot of back and forth over the next few years and the swings will continue to feel extreme. It may be important to keep this in mind when considering market action.

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

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 @ $106.18 limit. Based on short-term market outlook.

TGT - buy @ $47.56 limit - Based on system 11111. This one closed just under its 20ma. I'll put a stop under the most recent swing low at $46.79 to control risk.

Active Trades Table

none