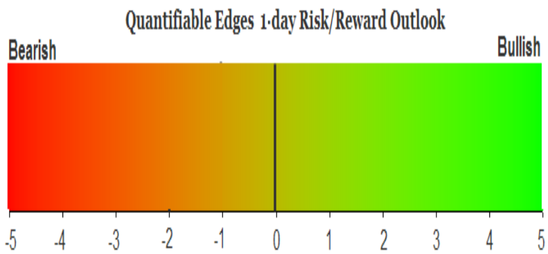
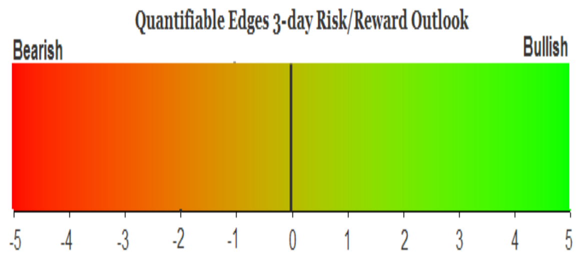
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 10, 2009 Volume 2 Issue 217

Market Overview





Tonight's Research Points

- Volume continues to suggest a short-term pullback is likely. Tonight it is SPY volume rather than NYSE volume that is hinting at the pullback.
- A breadth-thrust type signal was triggered today when the 2nd strong breadth day in the last 3 days took the market to new short-term highs. This suggests the market has a good chance of continuing to rally over the next few weeks.
- While the market is extremely overbought, the Aggregator remains neutral.

Short-term Outlook – updated 11/10

The Bottom Line

The breadth thrust pattern discussed in the Intraday Update this afternoon is dominating tonight's studies. Its strong positive expectations have kept the Aggregator from triggering a short signal. The market appears strongly overbought but dangerous on both sides currently.

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				
November 9, 2009	10-day high close on 10-day low vol	1-5 days	Bearish	-2.50%
Active - Long Term				
October 28, 2009	75% Up Issues 2 of 3 above 200 & 10 hi	1-20 days	Bullish	5.90%
Dropped Tonight				
November 9, 2009	***VIX goes from overbought to oversold***	***1-5 days***	***Bullish***	***1.50%***
November 6, 2009	***Nasdaq Up Vol % > 90%***	***1-3 days***	***Bullish***	***1.40%***
October 28, 2009	McClellan < -225, SPX > 200ma	1-9 days	Bullish	3.40%
November 3, 2009	Weak breadth bounce	1-4 days	Bearish	-4.00%

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

The Evidence

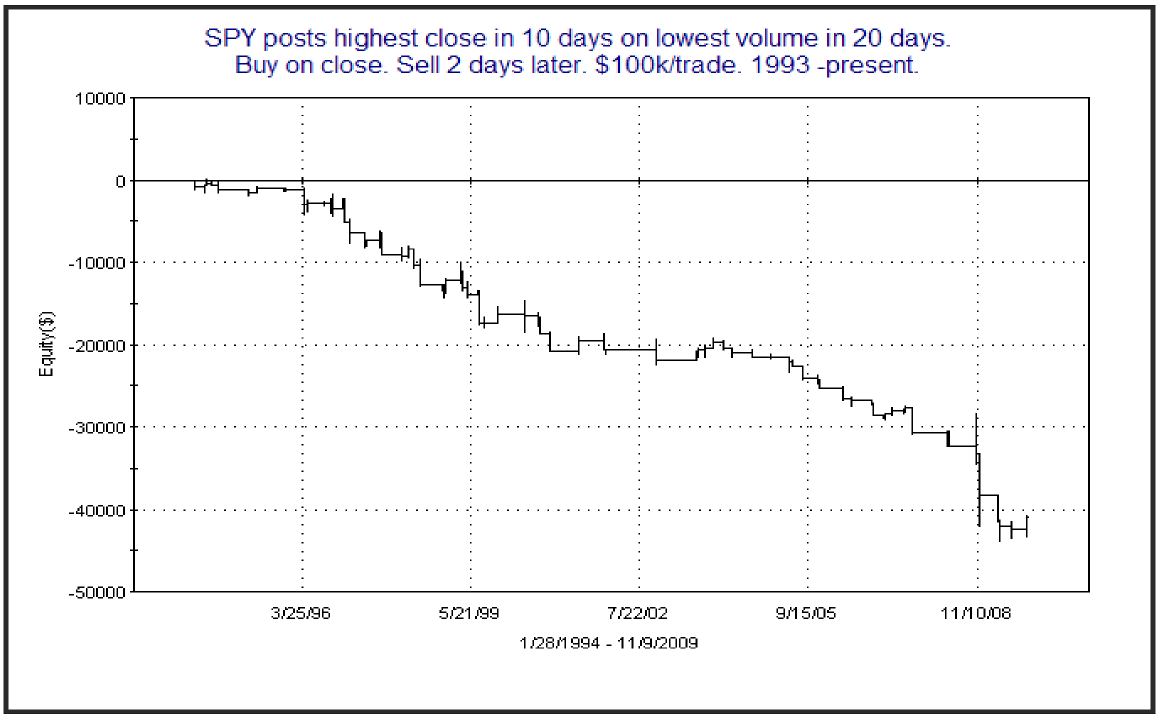
A gap up of about 0.75% never looked back and the market put in a solid trend day to the upside. The major indices all rose around 2%. Breadth was very strong. The NYSE Up Issues % came in at 84% and the Up Volume % at 94%. Volume rose, but remained well below average. SPY volume was especially weak and actually came in at the lowest level in over a month.

There were two studies identified by the Quantifinder tonight related to the volume in the SPY. Both studies were very similar to what we looked at last night. One looked at declining volume on a streak of higher closes. The other looked at 20-day volume lows when the market is in the upper end of its range. I changed this second one slightly to see how it looked when the SPY was at a 10-day high. Those results are below:

SPY posts highest close in 10 days on lowest volume in 20 days.
Buy on close. Sell X days later. $100k/trade. 1993 -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	-40,743.13	65	28	37	43.08	1,015.56	-1,869.70	0.54	0.41	-626.82
4	-45,330.78	67	30	37	44.78	841.68	-1,907.60	0.44	0.36	-676.58
3	-42,021.23	68	26	42	38.24	738.91	-1,457.93	0.51	0.31	-617.96
2	-40,913.21	71	24	47	33.80	582.64	-1,168.01	0.50	0.25	-576.24
1	-17,159.23	74	25	49	33.78	695.58	-705.08	0.99	0.50	-231.88

Here we see downside tendencies over the next few days. Most of the bearish edge occurs in the 1st 2 days though. Below is an equity curve that uses a 2-day exit.



What I find most appealing about this study is that it has been very consistent. This can be seen by the steady downward slope of the curve.

While I'd normally find this study compelling enough to include in the Aggregator, it is almost a carbon copy of last night's study that used the SPX and NYSE volume. Therefore, with last night's study already in place, I will leave this one out.

The most compelling directional evidence I found today was related to the strong breadth we've now seen on this recent run-up. I discussed it in detail in the Intraday Update sent out this afternoon. Below is an excerpt for those that did not have time to read it.

So far today breadth is coming in very strong. This is on the heels of very strong breadth on Thursday. The last time we saw a breadth thrust similar to this was on September 3rd and 4th. The September 8th Letter had some pertinent studies …

The primary study that is popping up again today is the following one that looks at 2 strong breadth days within a 3 day period. I've updated the stats so they're current.

NYSE Up Issues % > 75% in 2 of the last 3 days.
Buy SPX on close. Sell X days later. $100k/trade. 1970 - 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	89,459.96	40	28	12	70.00	4,609.88	-3,301.40	1.40	3.26	2,236.50
19	87,075.46	42	29	13	69.05	4,278.11	-2,845.37	1.50	3.35	2,073.23
18	81,916.79	42	31	11	73.81	3,760.11	-3,149.70	1.19	3.36	1,950.40
17	86,067.48	43	31	12	72.09	4,105.06	-3,432.44	1.20	3.09	2,001.57
16	73,894.66	43	31	12	72.09	3,923.25	-3,977.17	0.99	2.55	1,718.48
15	64,203.93	44	28	16	63.64	4,076.39	-3,120.94	1.31	2.29	1,459.18
14	59,887.22	44	33	11	75.00	3,277.68	-4,388.75	0.75	2.24	1,361.07
13	53,713.35	45	33	12	73.33	3,059.47	-3,937.43	0.78	2.14	1,193.63
12	37,168.94	46	30	16	65.22	3,153.11	-3,589.02	0.88	1.65	808.02
11	43,206.35	46	28	18	60.87	3,406.58	-2,898.76	1.18	1.83	939.27
10	52,734.13	46	30	16	65.22	3,393.43	-3,066.80	1.11	2.07	1,146.39
9	53,017.99	46	31	15	67.39	3,343.16	-3,374.66	0.99	2.05	1,152.57
8	46,809.38	46	31	15	67.39	2,865.58	-2,801.58	1.02	2.11	1,017.60
7	43,953.51	46	30	16	65.22	2,964.17	-2,810.72	1.05	1.98	955.51
6	39,231.62	47	31	16	65.96	2,438.24	-2,272.11	1.07	2.08	834.72
5	34,124.87	48	31	17	64.58	2,191.68	-1,989.25	1.10	2.01	710.93
4	40,302.82	50	31	19	62.00	1,988.23	-1,122.75	1.77	2.89	806.06
3	31,482.41	52	33	19	63.46	1,951.65	-1,732.73	1.13	1.96	605.43
2	15,377.11	58	35	23	60.34	1,348.63	-1,383.69	0.97	1.48	265.12
1	22,328.32	64	40	23	62.50	936.07	-657.15	1.42	2.48	348.88

Here we see that such breadth thrusts in general have often been decent predictors of more upside in the coming weeks – even as far out as 4 weeks.

In that September letter I also looked at a pattern that suggested breadth thrusts that achieve 10-day highs are more powerful than those that don't. That study used slightly *different parameters and required 2 strong days in a row. Today I decided to simply filter the above study and require a 10-day high. Those results are below:*

NYSE Up Issues % > 75% in 2 of the last 3 days. SPX posts the highest close in 10 days.
Buy SPX on close. Sell X days later. $100k/trade. 1970 - 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	102,417.76	34	26	8	76.47	5,165.92	-3,987.02	1.30	4.21	3,012.29
19	101,150.26	35	27	8	77.14	4,901.18	-3,897.69	1.26	4.24	2,890.01
18	92,858.90	35	28	7	80.00	4,282.54	-3,864.61	1.11	4.43	2,653.11
17	93,112.30	35	27	8	77.14	4,513.74	-3,594.85	1.26	4.24	2,660.35
16	87,824.59	35	27	8	77.14	4,377.94	-3,797.47	1.15	3.89	2,509.27
15	81,922.24	36	25	11	69.44	4,395.68	-2,542.70	1.73	3.93	2,275.62
14	72,203.58	36	28	8	77.78	3,587.51	-3,530.84	1.02	3.56	2,005.66
13	57,363.92	37	28	9	75.68	3,222.32	-3,651.22	0.88	2.75	1,550.38
12	52,043.21	38	27	11	71.05	3,197.10	-3,116.24	1.03	2.52	1,369.56
11	50,280.28	38	26	12	68.42	3,363.87	-3,098.37	1.09	2.35	1,323.17
10	61,384.75	38	28	10	73.68	3,344.91	-3,227.28	1.04	2.90	1,615.39
9	60,649.78	38	27	11	71.05	3,408.57	-2,852.87	1.19	2.93	1,596.05
8	49,655.21	38	27	11	71.05	2,911.69	-2,632.75	1.11	2.71	1,306.72
7	46,415.60	38	26	12	68.42	2,890.13	-2,393.98	1.21	2.62	1,221.46
6	41,016.53	39	28	11	71.79	2,372.79	-2,311.06	1.03	2.61	1,051.71
5	38,225.39	39	27	12	69.23	2,169.63	-1,696.22	1.28	2.88	980.14
4	31,674.55	41	25	16	60.98	1,992.73	-1,133.97	1.76	2.75	772.55
3	24,469.47	42	26	16	61.90	1,779.55	-1,362.43	1.31	2.12	582.61
2	13,723.11	48	29	19	60.42	1,244.58	-1,177.35	1.06	1.61	285.90
1	9,156.39	52	30	21	57.69	790.12	-692.72	1.14	1.63	176.08

So you can see here that a 10-day high is desirable and that returns were improved pretty much across the board using this filter.

Of course breadth thrusts may often occur in downtrends as volatility is extreme. I decided to filter out any instances that took place below the 200ma and have 1 more look.

NYSE Up Issues % > 75% in 2 of the last 3 days. SPX posts the highest close in 10 days. Close > 200ma. Buy SPX on close. Sell X days later. $100k/trade. 1970 - present.

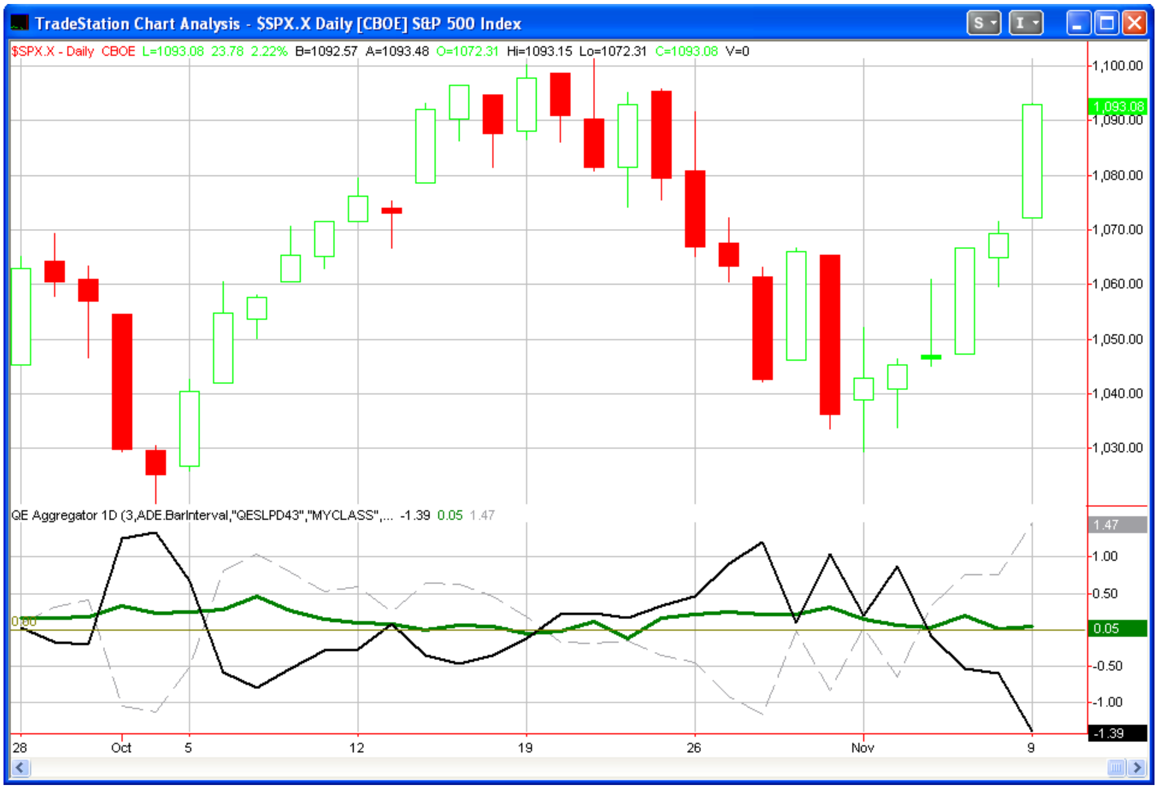
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	77,018.15	17	16	1	94.12	4,912.07	-1,575.00	3.12	49.90	4,530.48
19	73,506.97	18	16	2	88.89	4,822.86	-1,829.43	2.64	21.09	4,083.72
18	70,500.38	18	17	1	94.44	4,325.12	-3,026.67	1.43	24.29	3,916.69
17	66,931.52	18	17	1	94.44	4,293.64	-6,060.33	0.71	12.04	3,718.42
16	65,224.79	18	17	1	94.44	4,164.87	-5,578.02	0.75	12.69	3,623.60
15	56,697.24	18	15	3	83.33	4,217.67	-2,189.28	1.93	9.63	3,149.85
14	53,692.86	18	17	1	94.44	3,567.11	-6,948.06	0.51	8.73	2,982.94
13	51,871.16	19	17	2	89.47	3,442.08	-3,322.08	1.04	8.81	2,730.06
12	49,027.40	20	16	4	80.00	3,538.05	-1,895.37	1.87	7.47	2,451.37
11	48,665.82	20	16	4	80.00	3,487.71	-1,784.37	1.95	7.82	2,433.29
10	42,930.81	20	16	4	80.00	3,232.15	-2,195.91	1.47	5.89	2,146.54
9	43,224.10	20	16	4	80.00	3,276.12	-2,298.45	1.43	5.70	2,161.21
8	37,265.24	20	16	4	80.00	2,760.43	-1,725.40	1.60	6.40	1,863.26
7	35,883.17	20	15	5	75.00	2,750.28	-1,074.22	2.56	7.68	1,794.16
6	36,956.48	21	18	3	85.71	2,270.18	-1,302.27	1.74	10.46	1,759.83
5	30,217.95	21	16	5	76.19	2,093.29	-654.95	3.20	10.23	1,438.95
4	26,314.11	22	18	4	81.82	1,578.23	-523.53	3.01	13.57	1,196.10
3	17,797.99	22	16	6	72.73	1,382.97	-721.60	1.92	5.11	809.00
2	10,438.66	25	16	9	64.00	1,108.75	-811.25	1.37	2.43	417.55
1	6,086.89	27	17	10	62.96	692.62	-568.77	1.22	2.07	225.44

24 of 27 instances (89%) posted a close higher than the entry price within 3 days. All 27 instances posted a close > the entry price within 6 days.

These are fairly amazing results for a few simple filters… this would suggest more upside ahead.

Notable from the studies list is that 4 studies were removed this evening. One bullish and one bearish simply expired. Two other bullish studies hit their projected targets and were removed. This leaves us only with the short-term volume study from last night and the intermediate-term breadth study from today. And even with 3 bullish studies leaving the list the strength of the breadth thrust is keeping the net expectations positive.

The Aggregator chart is updated below.



Most notable on the Aggregator chart is that the black Differential line is now showing the SPX is more overbought versus expectation than it has been in a long time. The chart doesn't go back this far but the last time we saw values below the -1.39 reading tonight for the Differential was back in July. But while the market is now incredibly overbought, this hasn't translated into negative expectations. Last night I anticipated that it would but today was SO strong that it brought on studies suggesting this kind of strength often begets more strength. With positive expectations and the most overbought market in a long time, the Aggregator remains in neutral territory. Now is no time to start buying and it's also a dangerous time to get aggressively short. At this point it appears the next Aggregator entry might not come until the market manages a pullback.

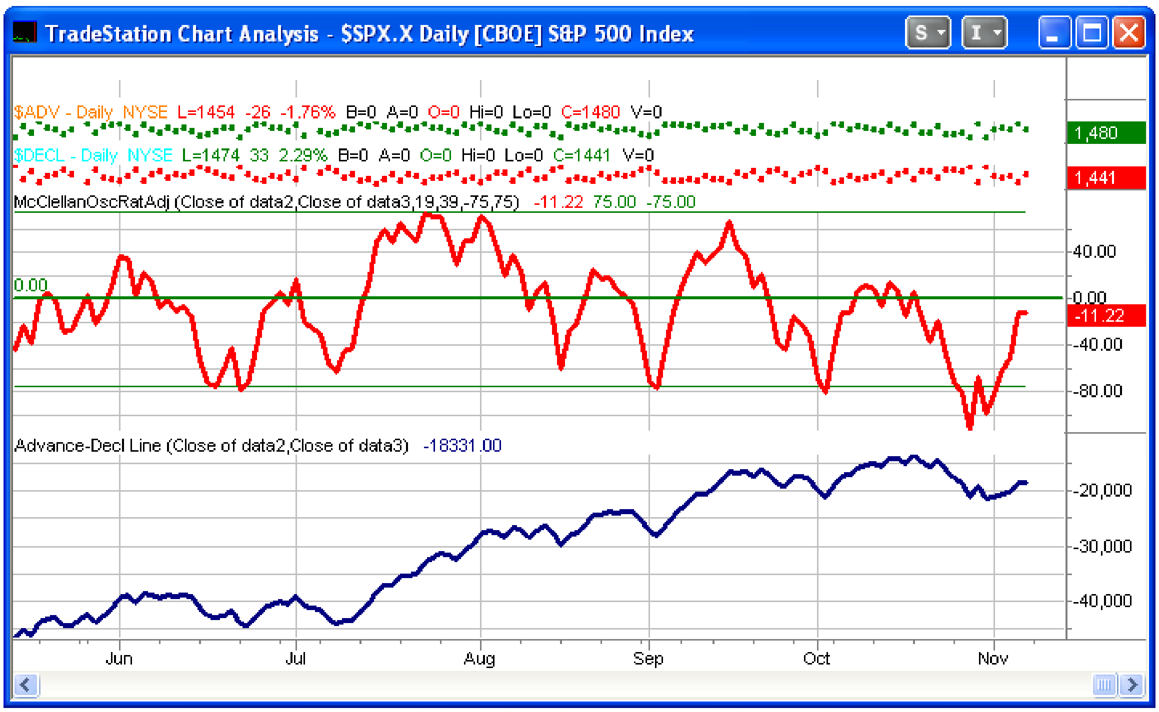
The weak volume studies continue to suggest a pullback is likely in the short-term. How deep that pullback is and whether it can last for more than 1 day will determine whether there is opportunity for a low-risk entry on the long-side. If even a shallow pullback arrives I will be looking for a fairly quick exit from the current small short position.

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/9 – neutral

In last weekend's intermediate-term outlook I discussed the extremely stretched state of the Ratio Adjusted McClellan Oscillator. That study suggested that selling had reached levels that normally shouldn't occur in an uptrend. The study also suggested the low of Friday October 30th could be a line in the sand. A move much below that level would mean a deeper decline lasting at least a few weeks was likely. If that line could hold, though, then the market might actually be able to begin a substantial rally over the next 4-5 weeks. So far so good as the market has risen 5 days in a row since then. I'll still be watching the low of the recent pullback as important. The short-term outlook is suggesting a pullback is likely early this week. Should the pullback hold above the recent swing low, then a bullish outlook would appear reasonable. A close below that level would suggest a bearish outlook. Those wishing to review last week's study may use the link below:

2009-11-02 QE Weekly Research Letter.pdf

I've shown a few breadth studies in recent weeks that looked at measures other than those included on the charts page. Based on subscriber requests, I've created a new chart on the charts page that from now on will show on a daily basis the Ratio Adjusted NYSE McClellan Oscillator and the NYSE Advance/Decline line. A copy of that chart is below.



The Ratio Adjusted McClellan Oscillator is the red line and the Advance / Decline line is blue. In the near future I will add a new page with a longer-term chart and research links similar to the other chart detail pages.

Most major tops have seen breadth divergences occur prior to the actual price peak. Of course it's entirely possible that the current rally could top out without breadth divergences that I'd noted were prevalent in past reports. To review the study that looked at divergent breadth action prior to significant tops see the October 12th Letter below.

2009-10-12 QE Weekly Research Letter.pdf

A top from here may or may not be considered "major" since the market is not near all-time highs. Still I'll continue to watch the New Highs and the A/D line for divergence clues. For now the uptrend remains in tact. A move below last weeks low or a new high that isn't soon accompanied by an expansion of New Highs and a breakout in the A/D line would suggest trouble ahead.

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.

None tonight.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Pr	% Gain/Lo	Stop	Notes
SPY(1/4)(s)	11/9/2009	$107.95	$109.57	-1.50%		short on open

I was worried I might be setting the limit on the gap up short entry a little low and expressed as much last night. Unfortunately the entry triggered by $0.05 and then got steamrolled. I'm not going to chase immediately. I'll watch the action early tomorrow and may institute an afternoon stop. Should we get a pullback as the volume studies are suggesting then I'll be quick to cover and keep the losses fairly small. I have no interest in adding to the short position.