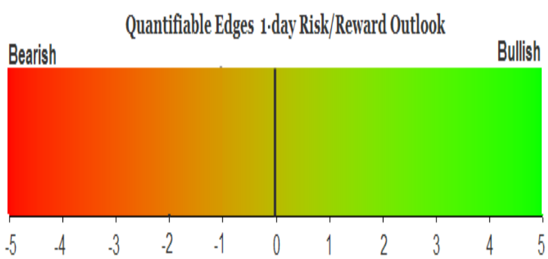
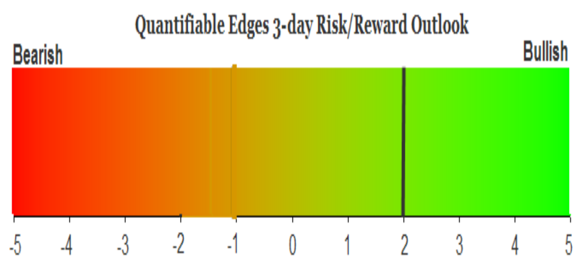
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

December 15, 2009 Volume 2 Issue 241

Market Overview





Tonight's Research Points

- SPX breakout to new highs short-term bullish, but just short-term.
- Confirmation by Nasdaq provides no discernable edge.
- Fed Day Wednesday seasonally bullish – especially from Tuesday's close to 2pm Wednesday.
- Aggregator System remains flat.

Short-term Outlook – updated 12/15

The Bottom Line

A new closing high and strong seasonality the next few days have net expectations slightly positive. Still, the market is overbought to the point that risks appear high. The sideline still appeals to me.

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				
December 15, 2009	SPX breakout to 50-high	1-3 days	Bullish	1.20%
December 14, 2009	December Op-Ex Week Bullish	1-5 days	Bullish	2.00%
December 14, 2009	SPY up 3 days on 3 days lower volume	1-3 days	Bearish	-1.70%
December 11, 2009	Nasdaq Up Issues < 40%. SPX Up.	1-3 days	Bearish	-2.20%
December 9, 2009	SPX down 1% & Declines 2x Advancers	1-9 days	Bullish	3.40%
December 9, 2009	SPX down 1% while SOX positive	1-6 days	Bullish	2.90%
Active - Long Term				
December 7, 2009	Nasdaq Leading S&P	int. term	Bullish	
December 2, 2009	VIX:VXV corsses below 0.9	2-5 months	Bearish	

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

The Evidence

The market went with the increasingly popular "gap up and slide sideways" move again today. That makes 3 in a row. The S&P 500 closed up 0.7%. The Nasdaq was up 1% and the Russell 2000 was up 1.6%. Breadth was solidly positive. The NYSE Up Issues % came in at 73% and the Up Volume % was 69%. Total volume increased slightly.

Though the intraday highs were not surpassed, the S&P and Nasdaq did both set new closing highs. They were the 1st closing highs since late November. Typically when the SPX breaks out to a new closing high after not making one for at least a couple of weeks, it leads to short-term follow through. I looked at this a few different ways – using both SPY and SPX and considering 50 and 200 day highs. All the results came out very similar. Below is one example.

SPX closes at a 50-day high. It had not done so for at least 10 days prior.
Buy 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	16,800.16	151	75	76	49.67	3,347.73	-3,082.63	1.09	1.07	111.26
19	41,914.39	154	83	71	53.90	3,175.16	-3,121.46	1.02	1.19	272.17
18	55,489.05	154	84	70	54.55	3,176.38	-3,018.95	1.05	1.26	360.32
17	40,568.47	154	84	70	54.55	3,017.93	-3,041.97	0.99	1.19	263.43
16	47,539.58	156	87	69	55.77	2,896.29	-2,962.87	0.98	1.23	304.74
15	48,537.19	158	86	72	54.43	2,860.83	-2,742.98	1.04	1.25	307.20
14	43,050.66	160	93	67	58.13	2,541.30	-2,884.93	0.88	1.22	269.07
13	48,402.75	161	89	72	55.28	2,563.73	-2,496.80	1.03	1.27	300.64
12	23,644.65	162	85	77	52.47	2,426.16	-2,371.15	1.02	1.13	145.95
11	22,062.78	165	84	81	50.91	2,449.68	-2,268.03	1.08	1.12	133.71
10	21,048.10	165	80	85	48.48	2,348.85	-1,963.06	1.20	1.13	127.56
9	30,395.36	165	86	78	52.12	2,075.65	-1,898.85	1.09	1.21	184.21
8	37,372.28	165	93	72	56.36	1,825.04	-1,838.28	0.99	1.28	226.50
7	55,124.80	165	91	74	55.15	1,788.13	-1,453.99	1.23	1.51	334.09
6	63,262.81	165	99	66	60.00	1,613.10	-1,461.12	1.10	1.66	383.41
5	64,843.77	165	95	70	57.58	1,664.41	-1,332.51	1.25	1.70	392.99
4	40,775.20	165	98	67	59.39	1,312.99	-1,311.91	1.00	1.46	247.12
3	51,505.81	165	100	65	60.61	1,213.75	-1,074.91	1.13	1.74	312.16
2	40,635.68	165	103	61	62.42	913.08	-875.59	1.04	1.76	246.28
1	29,212.89	165	102	62	61.82	561.37	-452.36	1.24	2.04	177.05

83% of instances closed higher than the entry price at some point in the next 5 days.

I find it interesting that the while the breakout typically is accompanied by short-term follow through, it doesn't carry over to the intermediate-term.

One thing I'm neglecting to look at in the above test is the fact that the Nasdaq also broke to a new closing high. Many traders might see this as "confirmation" of the S&P's closing breakout. I decided to check and see how much difference the Nasdaq confirmation made.

SPX closes at a 50-day high. It had not done so for at least 10 days prior. Nasdaq confirms by also making a 50-day high. Buy 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	45,041.46	86	47	39	54.65	3,358.18	-2,892.12	1.16	1.40	523.74
19	56,726.22	88	50	38	56.82	3,196.14	-2,712.66	1.18	1.55	644.62
18	65,150.65	88	51	37	57.95	3,194.35	-2,642.20	1.21	1.67	740.35
17	39,478.91	88	50	38	56.82	2,937.59	-2,826.34	1.04	1.37	448.62
16	39,594.99	88	53	35	60.23	2,739.87	-3,017.66	0.91	1.37	449.94
15	43,658.82	90	51	39	56.67	2,846.87	-2,603.37	1.09	1.43	485.10
14	48,716.32	91	58	33	63.74	2,472.48	-2,869.31	0.86	1.51	535.34
13	48,828.11	91	56	35	61.54	2,501.17	-2,606.79	0.96	1.54	536.57
12	34,145.71	91	53	38	58.24	2,427.59	-2,487.28	0.98	1.36	375.23
11	25,527.18	92	50	42	54.35	2,476.97	-2,340.99	1.06	1.26	277.47
10	16,943.66	92	47	45	51.09	2,313.18	-2,039.46	1.13	1.18	184.17
9	21,093.92	92	49	43	53.26	2,092.59	-1,894.02	1.10	1.26	229.28
8	18,210.85	92	54	38	58.70	1,780.46	-2,050.89	0.87	1.23	197.94
7	30,267.54	92	55	37	59.78	1,706.49	-1,718.63	0.99	1.48	329.00
6	31,437.18	92	59	33	64.13	1,539.25	-1,799.36	0.86	1.53	341.71
5	33,962.12	92	54	38	58.70	1,716.43	-1,545.39	1.11	1.58	369.15
4	16,495.32	92	58	34	63.04	1,152.65	-1,481.12	0.78	1.33	179.30
3	20,275.62	92	56	36	60.87	1,142.32	-1,213.72	0.94	1.46	220.39
2	15,435.56	92	57	35	61.96	889.76	-1,008.01	0.88	1.44	167.78
1	12,559.60	92	57	34	61.96	519.45	-501.44	1.04	1.74	136.52

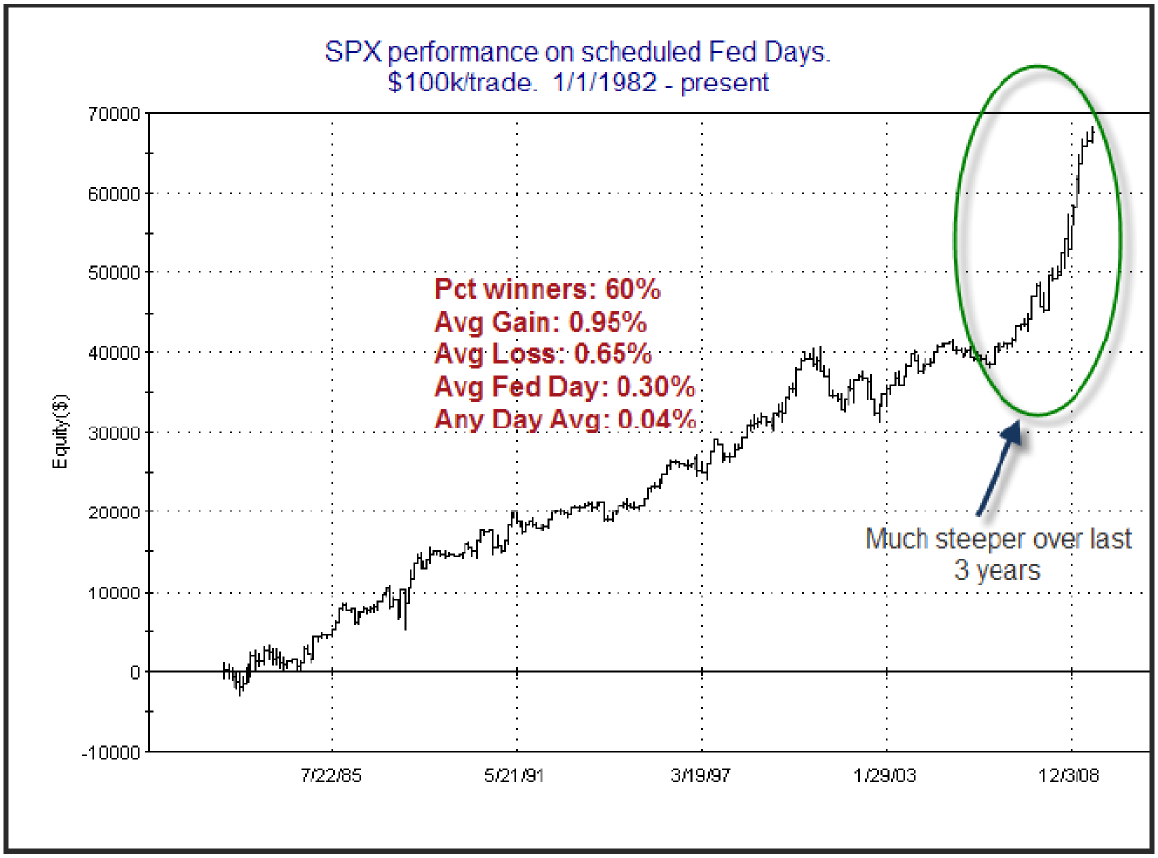
These results are almost identical to the first test, though with a reduced sample size. I compared several ways and kept coming up with the same answer. The confirmation seems to be worthless. It neither greatly enhances nor greatly detracts from results. This holds true both short and intermediate-term. Frankly this was a bit surprising to me since we know a leading Nasdaq has been a good sign historically.

The most significant studies in the Quantifinder today were related to the low SPY volume and the negative implications of that. I covered this with last night's research and there is already a study among the Active List pertaining to it. I see no reason to double up with this same indicator.

I mistakenly noted in the Intraday Quantifinder that Tuesday is a Fed Day. Being that it is a 2-day meeting Wednesday is the Fed Day. Apologies for any confusion.

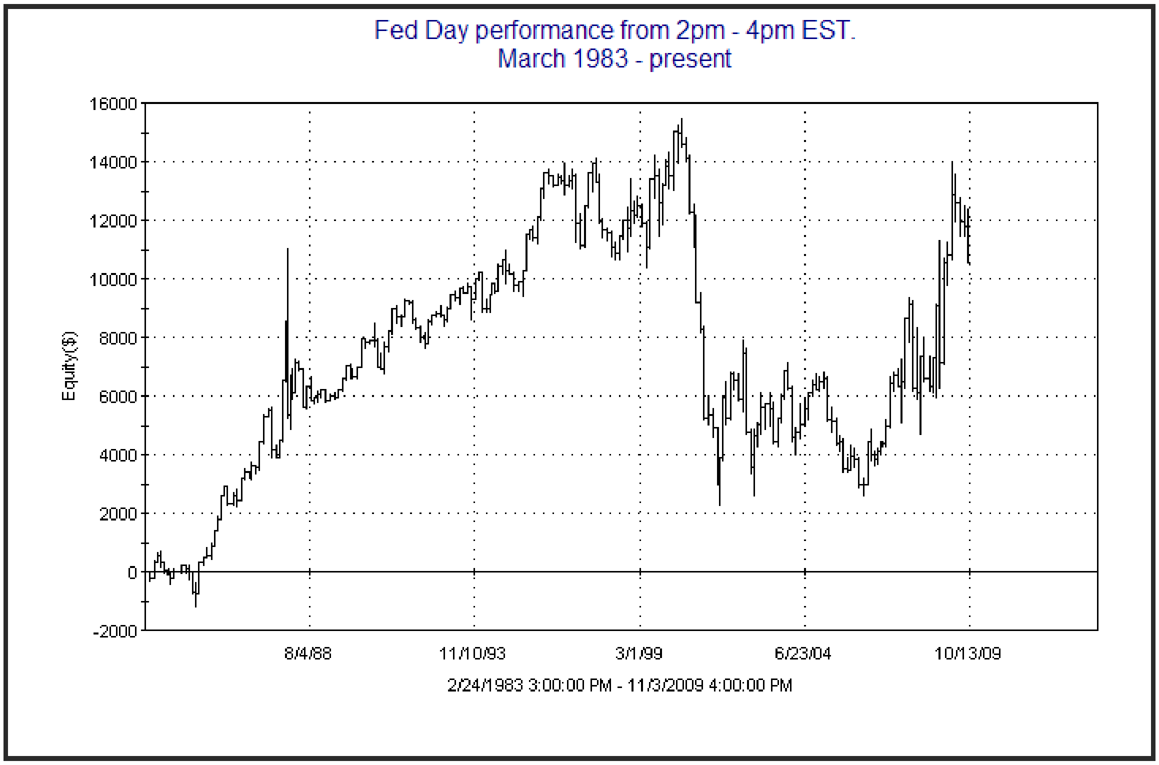
The excerpt below is from the 11/4/09 Subscriber Letter which was the last Fed day.

Speaking of the Fed, they help provide what appears to be the biggest edge tomorrow. Prior to the last Fed day I showed the following chart (not updated):



The September 23rd Fed day turned out to be a loser, but still the edge is quite strong. Since March of 1983, which is a far back as I have intraday data, the market has gained an additive 66% or so on Fed days. Tonight I decided to break out the return to view it pre and post-announcement.

Many people assume the reason Fed Days have done so well over the years is that the Fed comes often comes out and says or does something to placate the market. So it would stand to reason that much of the gains would occur after assurances from the Fed have been delivered shortly after 2pm EST. Let's first look at the 2pm -4pm EST period to see how the announcement may have affected the market over time.



From this chart it appears the edge has been mild and inconsistent with regards to trading after the announcement. Below are some stats to go along with the chart.

Fed Day performance from 2pm - 4pm EST.
March 1983 - present

TradeStation Performance Summary Collapse

All Trades

Total Net Profit	$10,558.68	Profit Factor	1.18
Gross Profit	$69,930.18	Gross Loss	($59,371.50)
Total Number of Trades	213	Percent Profitable	51.17%
Winning Trades	109	Losing Trades	104
Even Trades	0		
Avg. Trade Net Profit	$49.57	Ratio Avg. Win:Avg. Loss	1.12
Avg. Winning Trade	$641.56	Avg. Losing Trade	($570.88)
Largest Winning Trade	$3,451.02	Largest Losing Trade	($3,039.12)

These stats show that only a small portion of the gains have come after the announcement. So let's look at pre-announcement trading instead. I'll first show the stats this time.

SPX performance from the close the day before the Fed Day to 2pm of the Fed Day.
March, 1983 - present

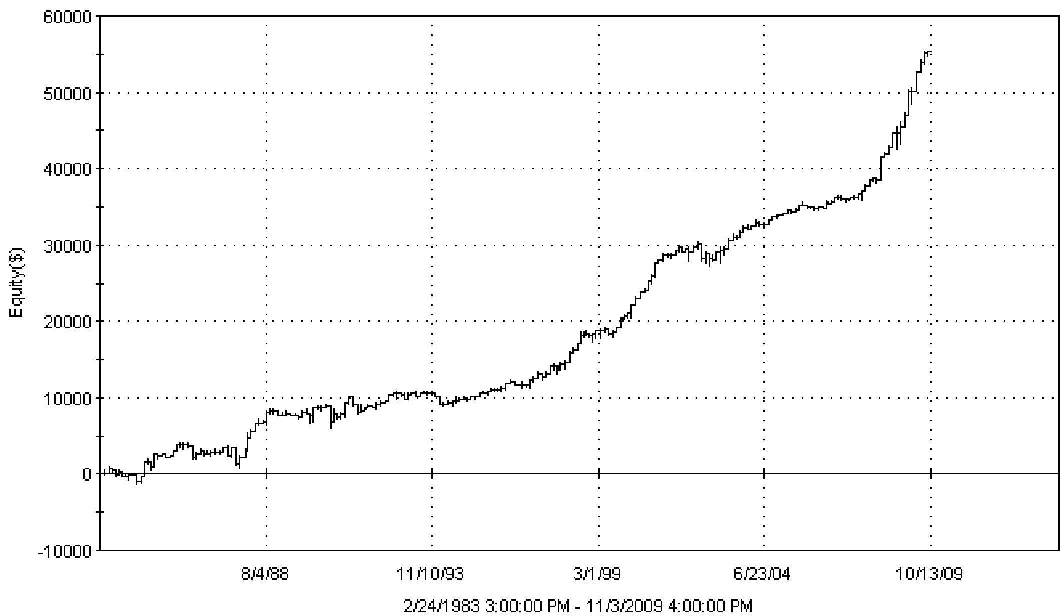
TradeStation Performance Summary Collapse

All Trades

Total Net Profit	$55,415.11	Profit Factor	3.14
Gross Profit	$81,370.53	Gross Loss	($25,955.42)
Total Number of Trades	212	Percent Profitable	68.87%
Winning Trades	146	Losing Trades	65
Even Trades	1		
Avg. Trade Net Profit	$261.39	Ratio Avg. Win:Avg. Loss	1.40
Avg. Winning Trade	$557.33	Avg. Losing Trade	($399.31)
Largest Winning Trade	$3,065.64	Largest Losing Trade	($2,009.28)

Profits during this time period are about 5 times the size of the 2-4pm period. The profit factor is very healthy and the % wins goes from 51% to 69%. But has the edge been consistent? Very much so. Here's the graph.

SPX performance from the close the day before the Fed Day to 2pm of the Fed Day.
March, 1983 - present



This suggests buying Tuesday's close and selling at 2pm Wednesday might hold a substantial edge.

I have updated the Aggregator chart below.

A minimal change again today on the Aggregator chart. For a while it appeared as though the green Aggregator line might flip negative, but it couldn't quite get there. This means the net expectation from the Active Studies remains just slightly bullish over the next 3 days. Monday's rise was strong enough to move the black Differential line a bit lower again today. The negative value illustrates the SPX outperformance versus expectations over the last few days. With both lines on opposing sides of zero the Aggregator configuration remains neutral. The Aggregator System is flat.

Tomorrow with the Fed Day studies looking to kick in for Wednesday the green Aggregator line is expected to remain positive. For the black Differential line to flip positive the SPX would need to close at 1,106.20 or lower. A strong move in either direction could generate a signal. The 3/10 Offset HV indicator remained extremely low today, suggesting a big move is likely soon. With the Fed meeting on Wednesday, that big move may wait until then to occur.

I may look to play the Fed day and perhaps get more aggressive should there be a sizable selloff tomorrow. Details in the trade ideas section below.

Intermediate-term Outlook (2 weeks – 2 months)– updated 12/14 –somewhat bullish

With the market still stuck in the range of the last several weeks, not much has happened to change my outlook. I can't imagine turning bearish unless there is a breakdown in price.

I've been watching breadth for a while now as both the Advance/Decline and the Net New High % has lagged over the last couple of months. There's been some improvement in the advance/decline line and it is just inches away from making new highs and confirming the rally. The new highs has a ways to go so even if the advance/decline breaks out here we'll need to keep an eye on new highs.

The Nasdaq/S&P 500 Relative strength indicator still favors the Nasdaq though the difference couldn't be smaller. If the S&P outperforms this week then it will surely take the lead back. You'll recall that the Nasdaq leading has been a much more favorable relationship since the inception of the Nasdaq. This was shown in detail in the blog in earlier this here. Click here to view that study.

The dollar rallied a bit this week and squarely broke through its 50-day ma. Despite this the S&P managed to close the week slightly higher. The dollar and S&P have had a strong inverse relationship since 2008. I ran a test back to December of 2007 to see how the S&P had performed other times when it managed to rise in spite of a dollar rally over a 5-day period. What I found was basically meaningless. During the bear market results showed downside over the next 1-2 weeks. During the recent rally the S&P followed such instances with more upside. You could test most anything over the same period and get similar results, so I'm not reading anything into it.

If the dollar continues to rise and the S&P can manage to hold up well I would interpret that as bullish.

In summary, price action and leadership remain bullish. Volume action could use some improvement. Breadth is close to ending its divergence. The S&P is holding up well despite a brief rally in the dollar and we are entering one of the most bullish times of the year from a seasonality standpoint. I see no convincing evidence to flip me bearish yet.

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 share at $111.87 LIMIT ON CLOSE. I'll look to play the Fed Day as long as we don't close up tomorrow. I anticipate selling this at 2pm Wednesday just prior to the announcement.

SPY - buy ¼ index share on SPX close below 1,106.21. I'll go a little heavier if an Aggregator signal actually kicks in, which would likely happen at this level. This lot I would hold beyond 2pm the next day.

Active Trades Table

none