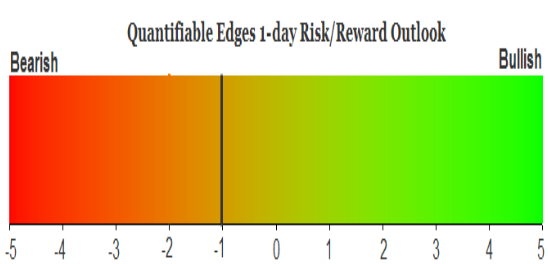
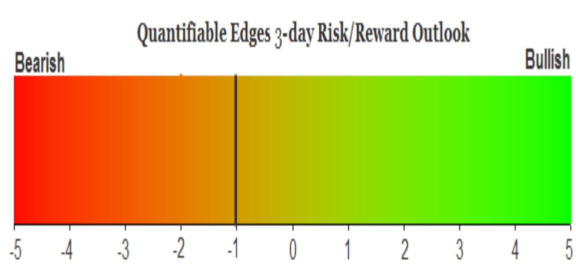
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 1, 2010 Volume 3 Issue 39

Market Overview





Tonight's Research Points

- The 1st day of March has not had a positive bias like other months have.
- The VIX persistently hitting new lows without accompanying SPX highs suggests short-term bearish implications for the SPX.
- The Aggregator System turned back to short at the close on Friday.
- The NDX Aggressive Trend Timer remains flat.

Short-term Outlook – updated 3/1
The Bottom Line

Neutral going into Friday has turned back to mildly bearish as of Friday's close. I'm wary at this point since the edge is so mild and the intermediate-term outlook is positive. It's a borderline short bias but a still a short bias for me at this point.

Summary of Recent Active Studies (see http://QuantifiableEdges.blogspot.com or Letters from listed dates for details)

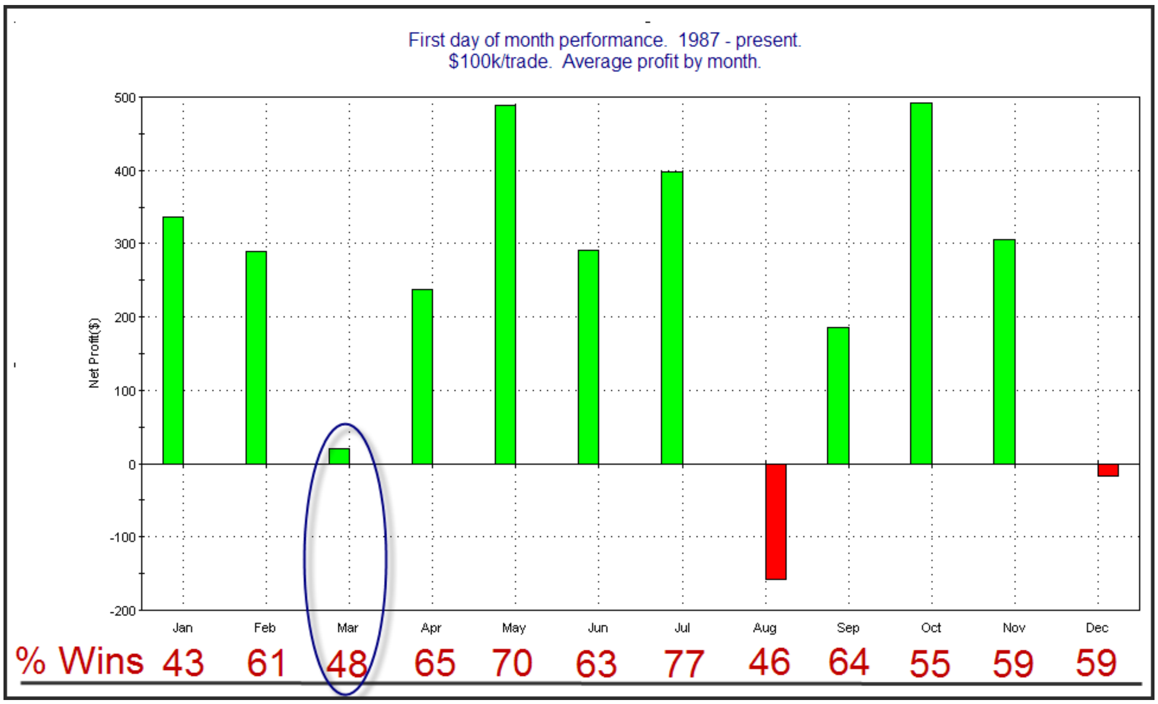
Study Date	Description	Time span	Bias	Avg Max Move
Active				
March 1, 2010	VIX 3 lows SPX 0 highs last 10 days	1-4 days	Bearish	-2.00%
February 24, 2010	1% drop and up issue % < 33.33%	1-9 days	Bullish	3.00%
February 23, 2010	SPY Lowest Vol 20 & Close > 10ma	1-5 days	Bearish	-2.10%
Active - Long Term				
February 22, 2010	VIX:VXV Ratio falls below 0.9	int. term	Bearish	
February 22, 2010	Good 5 days after FTD	int. term	Bullish	
February 16, 2010	Nasdaq/S&P RS Indicator Positive	int. term	Bullish	
February 12, 2010	IBD Follow Through Day	int. term	Bullish	
February 8, 2010	Worden %>200ma - %>40ma > 40	3 - 7 weeks	Bullish	
January 13, 2010	No bearish divergence at high	int. term	Bullish	
Dropped Tonight				
February 1, 2010	McClellan -60 for 6 days in a row	1-20 days	Bearish	

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

The Evidence

Friday saw some early morning selling followed by a sharp rebound. The bounce died out just after 10:30am and the range for the day was established. From there the market underwent generally quiet sideways trading. The indices finished mostly higher with the S&P up 0.1% and the Nasdaq 0.2% while the Russell lost 0.3%. Breadth was mildly positive as the NYSE Up Issues % finished at 59% and the Up volume % was 60%. NYSE volume rose to the highest level in a couple of weeks.

Typically we see the 1st day of the month provide a bit of a bullish tendency. This tendency really began to take hold in the late 80's when 401k plans started to become more popular and regular stock inflows began to occur at the beginning of the month. Last July I broke this edge out by month. Below is a copy of that chart (not updated).



I've circled the March stats. You can see that over the last 23 years March has been the 3rd worst both in terms of "% profitable" and in terms of "net profits". There have been 11 winners and 12 losers and the total profits have been right in line with long term drift. So while April – July should provide a bit of an upside edge at the beginning of the month, March just isn't showing it.

When the VIX is persistently hitting new lows while the SPX is failing to hit new highs it is normally a sign of too much complacency with a market that isn't that strong. In the 7/2/09 subscriber Letter I looked at this. I've updated that study's results below:

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
VIX makes a new 20-day low for at least the 3rd time in the last 10 days. SPX has 0 20-day highs in the last 10 days. Buy SPX on close. Sell X days later. $100k/trade. 1999 - present.										
20	-22,042.17	14	4	10	28.57	3,659.43	-3,667.99	1.00	0.40	-1,574.44
19	-22,423.41	14	4	10	28.57	3,425.35	-3,612.48	0.95	0.38	-1,601.67
18	-23,157.20	14	5	9	35.71	2,448.05	-3,933.05	0.62	0.35	-1,654.09
17	-25,310.12	14	4	10	28.57	2,609.03	-3,574.62	0.73	0.29	-1,807.87
16	-27,547.38	14	4	10	28.57	1,983.06	-3,547.96	0.56	0.22	-1,967.67
15	-23,015.83	14	4	10	28.57	2,403.86	-3,263.13	0.74	0.29	-1,643.99
14	-14,756.72	14	4	10	28.57	2,545.24	-2,493.77	1.02	0.41	-1,054.05
13	-9,804.17	14	5	9	35.71	2,066.37	-2,237.33	0.92	0.51	-700.30
12	-11,843.95	14	5	9	35.71	1,735.84	-2,280.35	0.76	0.42	-846.00
11	-8,728.78	14	6	8	42.86	1,666.08	-2,340.66	0.71	0.53	-623.48
10	-15,115.78	15	8	7	53.33	1,065.98	-3,377.66	0.32	0.36	-1,007.72
9	-17,874.46	15	7	8	46.67	1,147.24	-3,238.15	0.35	0.31	-1,191.63
8	-21,040.58	15	6	9	40.00	1,084.31	-3,060.71	0.35	0.24	-1,402.71
7	-19,134.78	15	6	9	40.00	1,416.22	-3,070.23	0.46	0.31	-1,275.65
6	-21,322.55	15	6	9	40.00	1,868.17	-3,614.62	0.52	0.34	-1,421.50
5	-22,688.00	16	6	10	37.50	1,732.61	-3,308.37	0.52	0.31	-1,418.00
4	-24,198.60	16	5	11	31.25	1,088.21	-2,694.51	0.40	0.18	-1,512.41
3	-13,498.92	16	5	11	31.25	1,584.84	-1,947.56	0.81	0.37	-843.68
2	-6,563.80	19	9	10	47.37	991.11	-1,548.38	0.64	0.58	-345.46
1	-3,074.59	24	12	12	50.00	737.95	-994.16	0.74	0.74	-128.11

This study suggests negative implications over both the short and intermediate-term. While instances aren't very large I did decide to break it out above and below the 200ma as I often do to see if there was a significant difference between the two. First let's look at times like the present when the SPX is in a long-term uptrend.

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
VIX makes a new 20-day low for at least the 3rd time in the last 10 days. SPX has 0 20-day highs in the last 10 days. SPX > 200ma. Buy SPX on close. Sell X days later. $100k/trade. 1999 - present.										
20	6,782.99	8	4	4	50.00	3,659.43	-1,963.68	1.86	1.86	847.87
19	4,908.31	8	4	4	50.00	3,425.35	-2,198.27	1.56	1.56	613.54
18	1,922.94	8	5	3	62.50	2,448.05	-3,439.10	0.71	1.19	240.37
17	41.24	8	4	4	50.00	2,609.03	-2,598.72	1.00	1.00	5.16
16	-2,844.74	8	4	4	50.00	1,983.06	-2,694.24	0.74	0.74	-355.59
15	-1,309.58	8	4	4	50.00	2,403.86	-2,731.25	0.88	0.88	-163.70
14	3,169.39	8	4	4	50.00	2,545.24	-1,752.89	1.45	1.45	396.17
13	162.03	8	4	4	50.00	1,996.54	-1,956.03	1.02	1.02	20.25
12	1,701.93	8	4	4	50.00	1,780.94	-1,355.46	1.31	1.31	212.74
11	2,173.29	8	5	3	62.50	1,593.38	-1,931.21	0.83	1.38	271.66
10	1,968.28	9	7	2	77.78	1,129.03	-2,967.45	0.38	1.33	218.70
9	-1,490.53	9	5	4	55.56	1,431.19	-2,161.62	0.66	0.83	-165.61
8	-4,937.59	9	4	5	44.44	1,199.97	-1,947.49	0.62	0.49	-548.62
7	-8,126.61	9	4	5	44.44	1,231.41	-2,610.45	0.47	0.38	-902.96
6	-8,651.82	9	4	5	44.44	1,695.10	-3,086.44	0.55	0.44	-961.31
5	-7,158.50	9	4	5	44.44	1,579.48	-2,695.28	0.59	0.47	-795.39
4	-7,645.02	9	4	5	44.44	1,244.99	-2,524.99	0.49	0.39	-849.45
3	-2,947.61	9	4	5	44.44	1,470.66	-1,766.05	0.83	0.67	-327.51
2	-1,365.14	11	6	5	54.55	921.17	-1,378.43	0.67	0.80	-124.10
1	-3,294.20	14	7	7	50.00	629.93	-1,100.53	0.57	0.57	-235.30

Here we see that there still seems to be a mild edge over the short-term. After that, though the results were mixed with no edge suggested.

Now let's take a look at the few times this occurred while the SPX was trading below the 200ma.

VIX makes a new 20-day low for at least the 3rd time in the last 10 days. SPX has 0 20-day highs in the last 10 days. SPX > 200ma. Buy SPX on close. Sell X days later. $100k/trade. 1999 - 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	-28,825.16	6	0	6	0.00	0.00	-4,804.19	0.00	0.00	-4,804.19
19	-27,331.72	6	0	6	0.00	0.00	-4,555.29	0.00	0.00	-4,555.29
18	-25,080.14	6	0	6	0.00	0.00	-4,180.02	0.00	0.00	-4,180.02
17	-25,351.36	6	0	6	0.00	0.00	-4,225.23	0.00	0.00	-4,225.23
16	-24,702.64	6	0	6	0.00	0.00	-4,117.11	0.00	0.00	-4,117.11
15	-21,706.25	6	0	6	0.00	0.00	-3,617.71	0.00	0.00	-3,617.71
14	-17,926.11	6	0	6	0.00	0.00	-2,987.69	0.00	0.00	-2,987.69
13	-9,966.20	6	1	5	16.67	2,345.68	-2,462.38	0.95	0.19	-1,661.03
12	-13,545.88	6	1	5	16.67	1,555.43	-3,020.26	0.51	0.10	-2,257.65
11	-10,902.07	6	1	5	16.67	2,029.58	-2,586.33	0.78	0.16	-1,817.01
10	-17,084.06	6	1	5	16.67	624.66	-3,541.74	0.18	0.04	-2,847.34
9	-16,383.93	6	2	4	33.33	437.39	-4,314.68	0.10	0.05	-2,730.66
8	-16,102.99	6	2	4	33.33	852.99	-4,452.24	0.19	0.10	-2,683.83
7	-11,008.17	6	2	4	33.33	1,785.83	-3,644.96	0.49	0.24	-1,834.70
6	-12,670.73	6	2	4	33.33	2,214.31	-4,274.84	0.52	0.26	-2,111.79
5	-15,529.50	7	2	5	28.57	2,038.89	-3,921.46	0.52	0.21	-2,218.50
4	-16,553.58	7	1	6	14.29	461.10	-2,835.78	0.16	0.03	-2,364.80
3	-10,551.31	7	1	6	14.29	2,041.57	-2,098.81	0.97	0.16	-1,507.33
2	-5,198.66	8	3	5	37.50	1,131.00	-1,718.33	0.66	0.39	-649.83
1	219.61	10	5	5	50.00	889.17	-845.24	1.05	1.05	21.96

There are really too few instances here to get too excited about an edge but you see that the negative intermediate-term results from the 1st test were all thanks to these few instances below the 200ma.

I've updated the Aggregator chart below.

With tonight's evidence the green Aggregator line has dipped ever so slightly back below zero. This indicates a very slight downside bias over the next 3 days based on the active studies. Meanwhile the black Differential line is squarely below 0, illustrating the SPX has handily outperformed expectations over the last few days. Both lines below 0 is considered a bearish configuration and has historically provided a downside edge. The Aggregator System went short at the close on Friday as was indicated on the Systems page.

Looking ahead the green Aggregator line is set up to remain positive over the next two days before turning back positive. Of course this doesn't include any studies that will arise in the next few days. Right now the Aggregator value is only slightly negative and the number of outstanding studies is relatively low. With this in mind new evidence will likely have a strong impact on the Aggregator value and could easily turn it either way over the next few days. The pivot level for the black Differential line will be 1,101.39 on Monday. In other words a SPX close at or below this level would flip the Differential positive. Should the market close above this number the Differential will remain negative.

As we entered Friday I wasn't expecting the Aggregator to turn negative. We had a slight bullish bias to the Aggregator line and beginning of the month coming up. A closer look in the afternoon brought about the evidence shown above. I'm not crazy about getting aggressively short in an environment where I have a bullish intermediate-term bias. What the Aggregator helps me to do though is to separate the evidence from my personal biases. I personally took a smaller than usual short position at the close and will not be looking to get aggressively short without more compelling evidence.

Intermediate-term Outlook (2 weeks – 2 months)– updated 3/1 – bullish

In the last couple of weeks we've seen several studies that have suggested intermediate-term implications. This week I am not seeing any new compelling intermediate-term evidence. There is a fair amount listed on the active studies list, though and I thought it might be a good idea to go over some of it.

I'll first discuss the bearish studies. The 1st one to note was from the February 1st letter. It examined the persistently weak breadth that was evident at the time as measured by the Ratio Adjusted McClellan Oscillator. Time has run out on that study as the month is now over. It was followed by another leg down but the market turned soon after and the intermediate-term influence was never exerted.

The other bearish study on the intermediate-term list is the VIX:VXV ratio dropping below 0.9. This study was discussed and updated in detail last week. It hasn't been a great timing device but rather has provided hints of downside to come. It also hasn't performed as well over the last year and a half as it had before that.

There are two bullish studies active that examined market breadth. The first was from mid-January. It suggested that since there was no breadth divergence when the January highs were hit that it was unlikely a significant top was being put in. The 2nd breadth related study was from the Feb 8th Letter and looked at the extremely low number of stocks trading above their 40ma versus those above their 200ma. This ratio suggested that the longer-term upmove was likely to re-exert itself over the shorter-term selloff.

There are also two studies listed that relate to IBD follow through days (FTD). February 11th gave us a valid follow FTD using the classic IBD definition which requires a 1% rise on higher volume. In recent years they have changed that requirement to several times and it now sits at 1.7% in their latest version. My testing suggested that changing of this requirement was not an effective idea. Interestingly, there still has not been a FTD based on the new definition but the Feb 11th classic FTD is still in effect. The other FTD study shown above was from last week and it suggested that the market rising in the week after the classic FTD was a good sign.

The last study shown above is the Nasdaq/S&P 500 Relative Strength Indicator which is shown on the charts page and updated each week. Currently the indicator is suggesting the Nasdaq is exerting relative strength over the S&P 500. This has historically been a good sign for the market and accounted for most of the gains in the S&P since 1971. Unfortunately we are not getting confirmation of this model from the NDX Aggressive Trend Timer System. February was a slow month for the system as it was in cash all but 1 day. It was a good 1 day as the NDX gained 1.29% on that day while the system was long. So while the Nasdaq/S&P RS Indicator from above is positive, I would prefer if it was confirmed by the NDX Aggressive Timer System.

So similar to last week we have a short-term sell signal from the Aggregator, but the intermediate-term still looks fairly bright. I still expect that we will be testing the January highs. For me to remove that expectation I'll need to see some additional bearish evidence of intermediate-term consequence or at the very least some elimination of the current bullish evidence.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Triggers

QCOM bought 1/3 position @ $37.12

New

QCOM @ buy 1/3 position @ $36.68

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 2(QCOM-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.

QCOM – buy1/3 position @ $36.68 limit. Based on the Catapult system. A reminder to anyone considering trading these signals: they have a tendency to be very volatile and stops are not used. Also the position will continued to be scaled into up to twice more on any repeat triggers. With all this in mind position sizing becomes very important from a risk management standpoint. Traders could also consider using options to control their risk and downside exposure.

SPY – short ¼ index position @ $110.74 limit. If not for a quick selloff in the last 5 minutes of the day the Spy would have closed above $111. I considered putting the limit in a little higher here but ultimately decided that if I'm only looking for a ¼ size position there is no need to get too picky.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
QCOM(1/3)	2/26/2010	$37.12	$36.68	-1.19%		Catapult