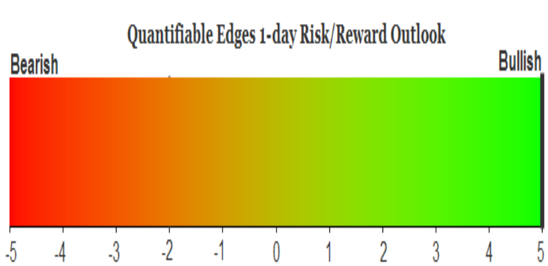
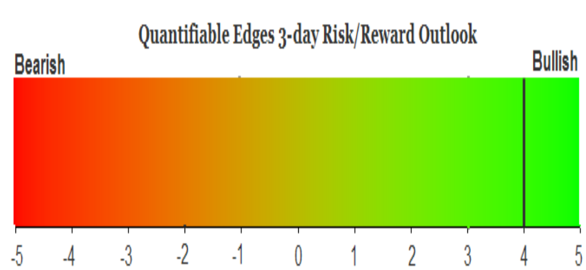
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

April 28, 2010 Volume 3 Issue 80

Market Overview





Tonight's Research Points

- Large price drops that finish near the bottom of the recent range during an uptrend often lead to a quick rebound.
- Large VIX spikes also often lead to a rebound.
- Also suggesting a bullish edge for tomorrow is the fact that it is a Fed Day.
- The Aggregator System remained went at the close.
- The NDX Aggressive Trend Timer stayed long at the close.

***Short-term Outlook** – updated 4/28*

The Bottom Line

A substantial amount of evidence is pointing towards a quick bounce. I'm positioning long to try and take advantage of it.

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	Avg MM - 1/3 Std Dev
Active					
April 28, 2010	2% drop to bottom 10% of range in uptre	1-7 days	Bullish		
April 28, 2010	VIX spikes > 25% above 10ma	1 day	Bullish		
April 28, 2010	Poor close prior to Fed Day	1 day	Bullish		
April 26, 2010	Low vol breakout to 50-day high	1-3 days	Bullish	1.30%	1.00%
Active - Long Term					
April 26, 2010	No breadth divergence at new high	int. term	Bullish		
April 19, 2010	1st drop below 10ma in long time	int. term	Bullish		
April 13, 2010	Ttl Put/Call 40-low. SPX no 0.5% up.	1-5 weeks	Bearish	-4.90%	-3.30%
April 6, 2010	SPX and TNX hit 50-day closing highs	int. term	Bearish		
February 16, 2010	Nasdaq/S&P RS Indicator Positive	int. term	Bullish		
Dropped Tonight					
April 26, 2010	***SPX & VIX up 2 days in row / on Fri***	***1-2 days***	***Bearish***	***-1.00%***	***-0.80%***

If the avg max move – 1/3 Std Dev is achieved the study will appear in ***bold italic blue*** and no longer be active.

The Evidence

The market took a nosedive Tuesday. It started before the open and it ended at the close, with a few brief bounces along the way. The major indices all closed down hard. The SPX and Russell 2000 both closed down between 2.3% and 2.4% while the Nasdaq lost just over 2%. Breadth was negatively lopsided as you would expect with the NYSE Up Issues % finishing at 16% and the Up Volume % just barely over 5%. Total NYSE volume spiked much higher but fell just short of the level achieved on the 4/16 selloff.

The Quantifinder showed a large number of bullish studies this evening. No time and no need to go through all of them. Instead I chose a few of the more substantial ones to highlight.

From a price standpoint alone, the action was extreme enough that a rebound typically follows almost immediately. On their own, 2% drops in uptrends tend to carry a bullish edge. Below is a study from the 10/2/2009 Subscriber Letter that shows this. The stats have not been updated.

SPX closes down 2% and above its 200ma.
Buy on close. Sell X days later. $100k/trade. 10/20/87 - 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	55,693.30	41	26	15	63.41	3,436.88	-2,244.37	1.53	2.65	1,358.37
9	60,201.45	42	29	13	69.05	3,126.33	-2,343.25	1.33	2.98	1,433.37
8	63,767.80	43	28	15	65.12	3,401.21	-2,097.73	1.62	3.03	1,482.97
7	43,059.71	43	27	16	62.79	2,926.30	-2,246.90	1.30	2.20	1,001.39
6	38,578.79	43	25	18	58.14	2,927.84	-1,923.17	1.52	2.11	897.18
5	32,569.12	43	22	21	51.16	2,900.55	-1,487.77	1.95	2.04	757.42
4	30,747.98	44	23	21	52.27	2,699.57	-1,492.48	1.81	1.98	698.82
3	24,720.84	44	25	19	56.82	2,061.71	-1,411.68	1.46	1.92	561.84
2	22,660.50	45	29	16	64.44	1,584.91	-1,456.37	1.09	1.97	503.57
1	19,099.83	46	33	13	71.74	908.33	-836.55	1.09	2.76	415.21

Adding filters that require the selloff to finish the day weakly and at the lower end of its 10-day range generate even more compelling results. This next study is from the 11/2/09 Letter and the stats HAVE been updated.

SPY drops more than 2%, closes at a 10-day low and above its 200ma. Close is in bottom 10% of daily range. 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
10	40,970.20	17	11	6	64.71	4,645.48	-1,688.34	2.75	5.04	2,410.01
9	48,960.10	19	15	4	78.95	3,873.23	-2,284.60	1.70	6.36	2,576.85
8	56,444.93	19	16	3	84.21	3,928.83	-2,138.80	1.84	9.80	2,970.79
7	53,891.72	19	17	2	89.47	3,430.15	-2,210.42	1.55	13.19	2,836.41
6	47,327.94	19	16	3	84.21	3,108.90	-804.83	3.86	20.60	2,490.94
5	40,716.61	19	15	4	78.95	2,964.04	-935.99	3.17	11.88	2,142.98
4	30,820.23	19	15	4	78.95	2,480.57	-1,597.06	1.55	5.82	1,622.12
3	33,548.69	19	15	4	78.95	2,456.00	-822.82	2.98	11.19	1,765.72
2	24,929.00	19	15	4	78.95	1,944.13	-1,058.24	1.84	6.89	1,312.05
1	18,914.87	19	17	2	89.47	1,195.65	-705.63	1.69	14.40	995.52

All 19 instances closed above the entry price in one of the next 2 days.

As you can see there has not only been a bounce within 2 days in every instance but the bounce has typically followed through over the next several days as well. This suggests that a selling climax has quickly been achieved and that the move higher will often reassert itself very shortly.

Climactic activity can be seen in other ways than just looking at price. The VIX is often referred to as the "fear index". Sharp moves upwards often signal highly emotional (and overzealous) selling. On Tuesday the VIX spiked up to more than 25% above its 10-day moving average. Spikes of such magnitude are rare when the SPX is trading above its 200ma. The study below is also from the 11/2/09 Letter.

VIX crosses over 25% above 10ma. SPX close > 200ma. Buy SPX on close. Sell X days later. $100k/trade. 1990 - 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	16,163.14	15	9	6	60.00	2,524.25	-1,092.51	2.31	3.47	1,077.54
4	18,246.71	15	10	5	66.67	2,260.75	-872.16	2.59	5.18	1,216.45
3	14,583.73	15	12	3	80.00	1,428.72	-853.62	1.67	6.69	972.25
2	15,733.56	15	11	4	73.33	1,571.64	-388.62	4.04	11.12	1,048.90
1	15,961.16	15	14	1	93.33	1,187.50	-663.78	1.79	25.05	1,064.08

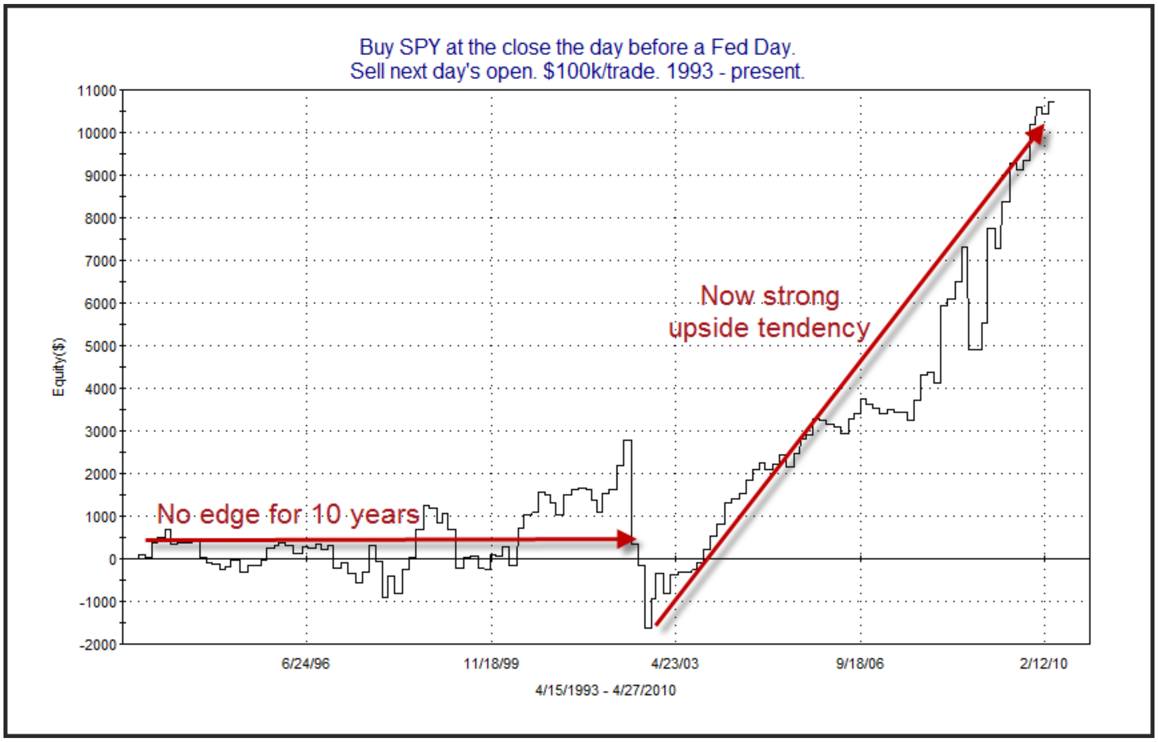
The one instance that didn't close higher the next day was 5/17/06. It didn't close above the trigger price until 6 days later. The max intraday drawdown was about 2.5%

We also see here that the reaction has consistently been an immediate bounce. And even the 1 instance that didn't bounce the next day didn't suffer any huge drawdown.

Whether you're looking at a price drop or a VIX spike the message is the same. Tuesday's move was sharp enough that in the past similar moves have almost always been followed by an immediate bounce.

It's also interesting that tomorrow is a Fed Day. The last couple of nights I mentioned how a selloff into Wednesday's Fed Day might allow for a nice buying opportunity. One of the SPY trade ideas I listed last night was based on a possible Fed Day trade. And as it turned out, we now actually have that selloff that loomed as a possibility. In the past I've shown how the biggest part of the Fed Day edge occurs between the close of the day before up until the actual announcement just after 2pm. After 2pm the reaction to the Fed is inconsistent, but has not added substantially to the Fed Day results over the last several years. Tonight I decided to break down the edge by time of day in a little more detail. First let's look at the overnight.

The chart below shows the overnight profits and losses in SPY since its inception in 1993 on the night before a Fed Day.



As you can see up until November of 2002 there was no bullish tendency in the overnight. Since that time there's been a substantial edge. The performance stats below show just how substantial the edge has been since late 2002.

Buy SPY at the close the day before a Fed Day.
Sell next day's open. $100k/trade. 11/2002 - present.

TradeStation Performance Summary Collapse

All Trades

Total Net Profit	$12,352.63	Profit Factor	3.35
Gross Profit	$17,601.61	Gross Loss	($5,248.98)
Total Number of Trades	60	Percent Profitable	70.00%
Winning Trades	42	Losing Trades	18
Even Trades	0		
Avg. Trade Net Profit	$205.88	Ratio Avg. Win:Avg. Loss	1.44
Avg. Winning Trade	$419.09	Avg. Losing Trade	($291.61)
Largest Winning Trade	$2,212.21	Largest Losing Trade	($2,404.48)

So as you can see the overnight session has typically gotten the market off to a good start over the since late 2002. I also looked at action on the Fed Day. Where previously I had only broken it out as either pre-2pm or post-2pm tonight I decided to break it out by ½ hour segments to see if there was anything more to be learned. My intraday data was good into around mid-1998 so I elected to just start this test as of 1/1/99.

Half-hourly performance on day of Fed meeting from 9:30am - 4pm.
$100k/trade. 1999 - present. (Bar 0 = 9:30am, Bar 12 = 3:30pm)

Fed Day Intraday: barentry	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
12	-6,004.52	88	47	41	53.41	322.52	-516.17	0.62	0.72	-68.23
11	-5,083.09	89	38	50	42.70	350.67	-368.17	0.95	0.72	-57.11
10	13,165.95	89	54	35	60.67	449.86	-317.89	1.42	2.18	147.93
9	-5,026.91	89	41	48	46.07	397.36	-444.14	0.89	0.76	-56.48
8	1,028.19	89	47	40	52.81	133.18	-130.78	1.02	1.20	11.55
7	4,923.34	89	53	33	59.55	125.18	-51.85	2.41	3.88	55.32
6	2,461.91	89	47	39	52.81	107.42	-66.33	1.62	1.95	27.66
5	-1,860.48	89	38	47	42.70	117.37	-134.48	0.87	0.71	-20.90
4	4,897.32	89	47	38	52.81	198.80	-117.01	1.70	2.10	55.03
3	776.64	89	53	33	59.55	106.32	-147.22	0.72	1.16	8.73
2	4,403.68	89	53	33	59.55	177.69	-151.94	1.17	1.88	49.48
1	9,030.34	89	55	31	61.80	257.29	-165.18	1.56	2.76	101.46
0	5,471.87	89	57	30	64.04	231.97	-258.36	0.90	1.71	61.48

In general what we see here is that the best action often occurs early in the day. After the first 60-90 minutes you have drifting, choppy action going into the announcement. The announcement has brought in some volatile movement which over time has resulted in slight downside.

These last few studies should help to explain why, if I'm looking to trade the Fed Day, I like to get long at the close the day before and be out by the time the announcement arrives.

Likely partially due to the fact that Fed Days have generally been positive, strong selloffs the day before have been uncommon. So one other study I ran tonight looks at other times the SPX sold off at least 1% on the day before a Fed Day. First I'll show the general results.

SPY closes down over 1% on the day before a Fed Day.
Buy on close. Sell next day's close. $100k/trade. 1994 - present.

TradeStation Performance Summary Collapse

All Trades

Total Net Profit	$14,992.43	Profit Factor	9.86
Gross Profit	$16,685.22	Gross Loss	($1,692.79)
Total Number of Trades	13	Percent Profitable	76.92%
Winning Trades	10	Losing Trades	3
Even Trades	0		
Avg. Trade Net Profit	$1,153.26	Ratio Avg. Win:Avg. Loss	2.96
Avg. Winning Trade	$1,668.52	Avg. Losing Trade	($564.26)
Largest Winning Trade	$4,704.07	Largest Losing Trade	($1,141.01)

The stats her are heavily lopsided in favor of the bulls. Below I've listed all occurrences.

SPY closes down over 1% on the day before a Fed Day. Buy on close. Sell next day's close. $100k/trade. 1994 - present.				
Date/Time	**Signal**	**Price**	**% Profit**	**Run-up DrawDown**
12/18/95	Buy	$60.63	1.07%	$1,187.28
12/19/95	Sell	$61.28		($82.45)
12/16/96	Buy	$72.56	0.54%	$992.16
12/17/96	Sell	$72.95		($937.04)
12/10/01	Buy	$114.38	(0.20%)	$1,171.16
12/11/01	Sell	$114.15		($419.52)
01/29/02	Buy	$110.28	1.44%	$2,817.66
01/30/02	Sell	$111.87		($1,703.28)
05/06/02	Buy	$105.47	(0.35%)	$805.80
05/07/02	Sell	$105.10		($540.36)
06/25/02	Buy	$97.56	0.16%	$604.75
06/26/02	Sell	$97.72		($2,429.25)
12/09/02	Buy	$89.50	1.34%	$1,787.20
12/10/02	Sell	$90.70		$0.00
01/27/04	Buy	$114.68	(1.14%)	$522.60
01/28/04	Sell	$113.37		($1,515.54)
03/15/04	Buy	$111.20	0.53%	$773.14
03/16/04	Sell	$111.79		($323.64)
03/17/08	Buy	$128.30	4.15%	$4,198.81
03/18/08	Sell	$133.63		$0.00
09/15/08	Buy	$120.09	1.67%	$1,855.36
09/16/08	Sell	$122.10		($2,570.88)
12/15/08	Buy	$87.75	4.71%	$4,863.53
12/16/08	Sell	$91.88		$0.00
08/11/09	Buy	$99.73	1.07%	$1,833.66
08/12/09	Sell	$100.80		($220.44)

While Fed Days have had a strong upside bias, many of the big moves prior to these days occurred at times when the market was in a downtrend and the environment was more volatile in general. Often when the market is trading in a difficult environment the Fed/government will try and placate the market. They want to "save" it and look good for their supporters. The market has had a massive run over the last 13 months and the current situation is much different than many of those other instances. In fact, you could say the opposite now is true. The Fed/government still wants to look good, but they are now doing it by going after Wall St. (specifically Goldman) instead of placating them. In other words, the "help" that is often present in making Fed Days bullish isn't present this time. I'm betting even without this extra incentive we still get a move up tomorrow, but just a little something to keep in mind as you formulate your plan. It's also worth noting that the selloff may partially be attributed to European debt struggles, which is outside of the Fed's jurisdiction.

I've updated the Aggregator chart below.

The Aggregator chart moved into a very bullish formation this evening. The green Aggregator line spiked up with all the strongly bullish studies discussed tonight. This shows that the net expectations over the next few days are now strongly positive. The black Differential line is illustrating the fact that the SPX has strongly underperformed expectations over the last few days. Both the positive expectations and the SPX underperformance are at levels we haven't seen for some time. This suggests a strongly bullish short-term edge. The Aggregator System went long at the close and I traded along with it.

Looking ahead the green Aggregator line is currently set up to remain positive for the near future. Of course most of the studies will be expiring tomorrow so any new bearish studies could quickly and substantially affect the Aggregator value. One thing to watch for at this point is the strength of any bounce should we get one. Often weak bounces may have a tendency to roll over while strong ones gain momentum and continue higher. The Differential pivot level tomorrow will be 1219.90. In other words it will take an SPX close at or above 1,219.90 in order to move the black Differential line into negative territory. This would take a rally of over 3% tomorrow to achieve this level, which seems unlikely.

In the trade ideas section below I took some exposure this afternoon based on last night's trade ideas. I will look to add some more exposure Wednesday.

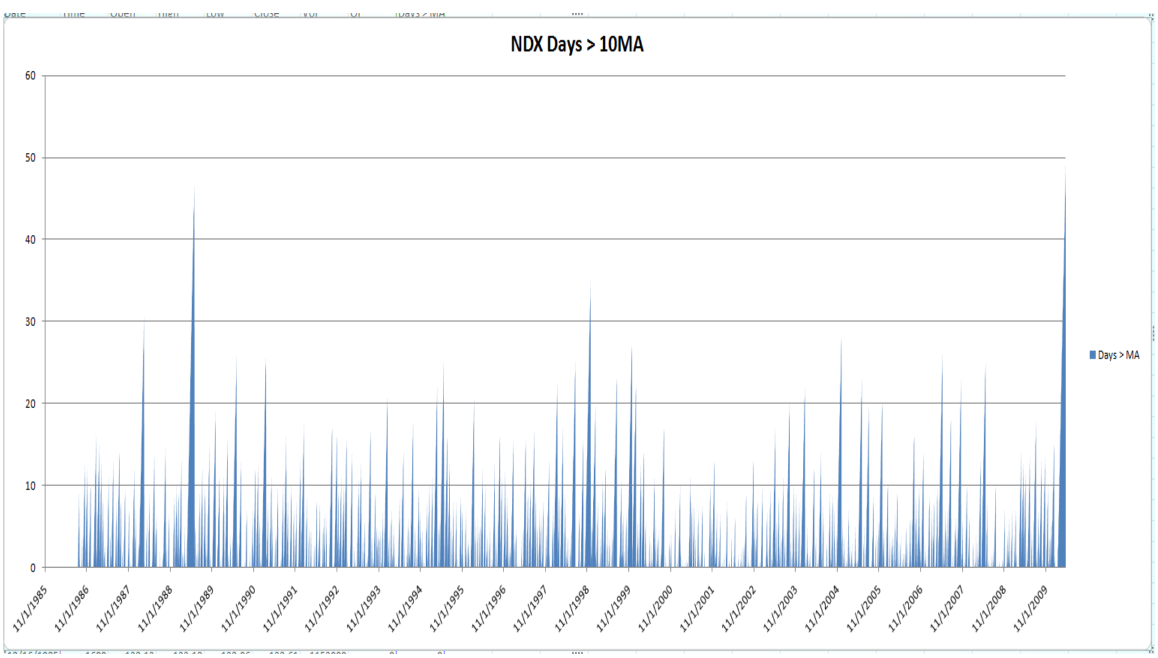
Intermediate-term Outlook (2 weeks – 2 months)– updated 4/26 somewhat bullish
A few times recently I discussed the incredible string of days the SPX went without closing below its 200ma. Today I will show the NDX and the Dow streaks. First I'll review my comments from last week.

Another notable about Friday's selloff that demonstrates how persistent the uptrend has been is the fact that it caused the SPX to close below the 10ma for the 1st time since February 12th. That streak consisted of 42 trading days above the 10ma before Friday. In the 3/22/10 Letter I discussed the fact that the SPY had gone more than 25 days above its 10ma. (The SPY streak was broken on 3/26 after going 30 days.) In that Letter I showed the 5 other times since 1993 that SPY had gone at least 25 days above the 10ma. My conclusion after viewing the charts was the following…" Strong and persistent upside movement like we have seen lately hasn't just ended and lead to an immediate correction. The 1st dip has always been just that – a dip. New highs were always made in short order." With this Letter already quite long I decided not to reproduce those charts again. Instead, if you would like to view them you may find the in the intermediate-term section of the 3/22 Letter which I have provided a download link to below:

2010-03-22 QE Weekly Research Letter.pdf

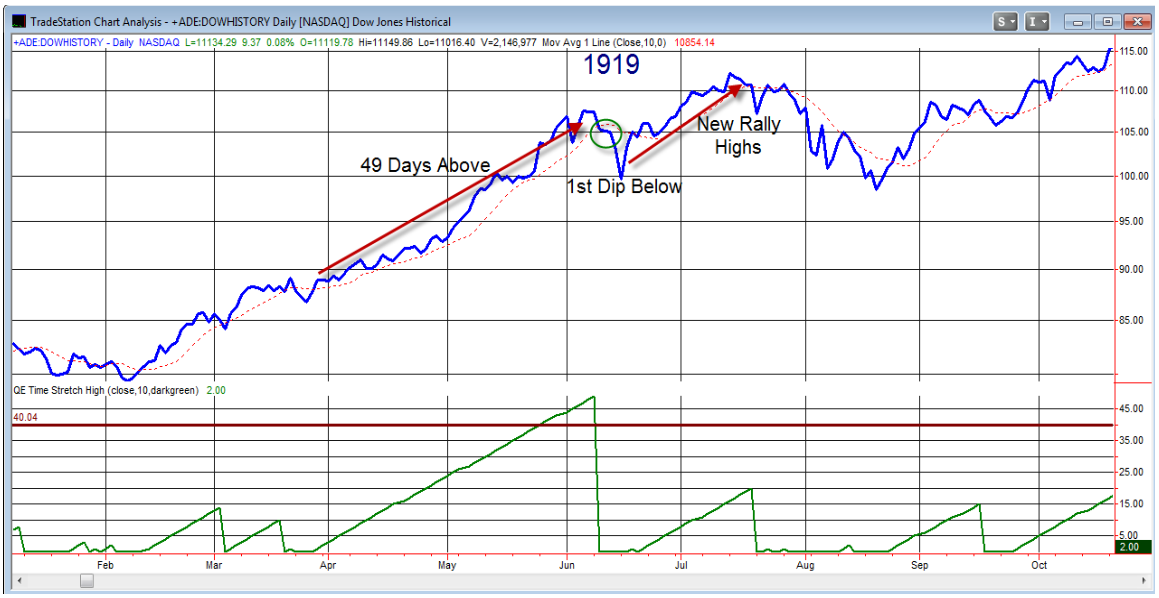
Along these lines this weekend I looked for other times the SPX closed above the 10ma for at least 40 days in a row. Looking back to 1960 there were only 4 other instances – the most recent occurring in 1972. The dates when the other 4 instances finally dipped below the 10ma were Feb 1961, Oct 1968, Feb 1971, and Jan 1972. In looking at those instances I am drawn to the same conclusion as the 3/22 study referenced above. Persistent strength never just ended on that 1st pullback. The market went on to make new highs each time and the rally continued.

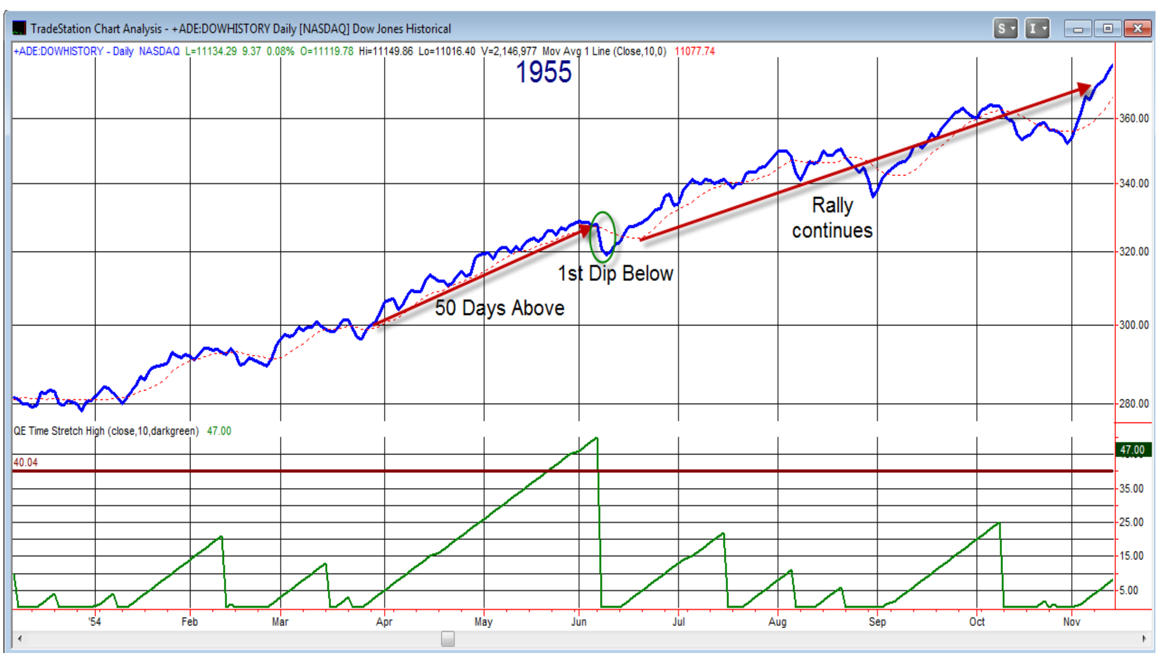
The NDX and the Dow STILL haven't dropped below their 10-day ma's. For the NDX the streak is now 50 days. The DIA is also 50, but the cash Dow is "just" 48 days. For the NDX this is the longest streak since its inception in 1986. Below is a chart that shows the number of days the NDX has spent above it 10ma at any point in time.

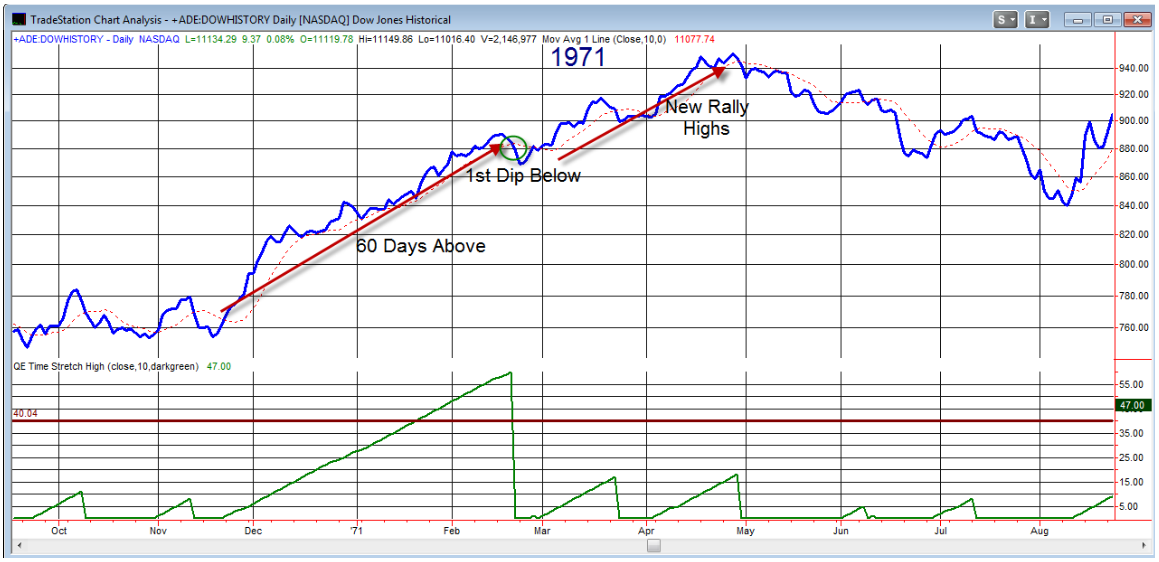


It's a little difficult to read when try to jam so much history into a small area, but the spike on the right is the current count and it is up to 50. The previous high lasted 47 days in 1989.

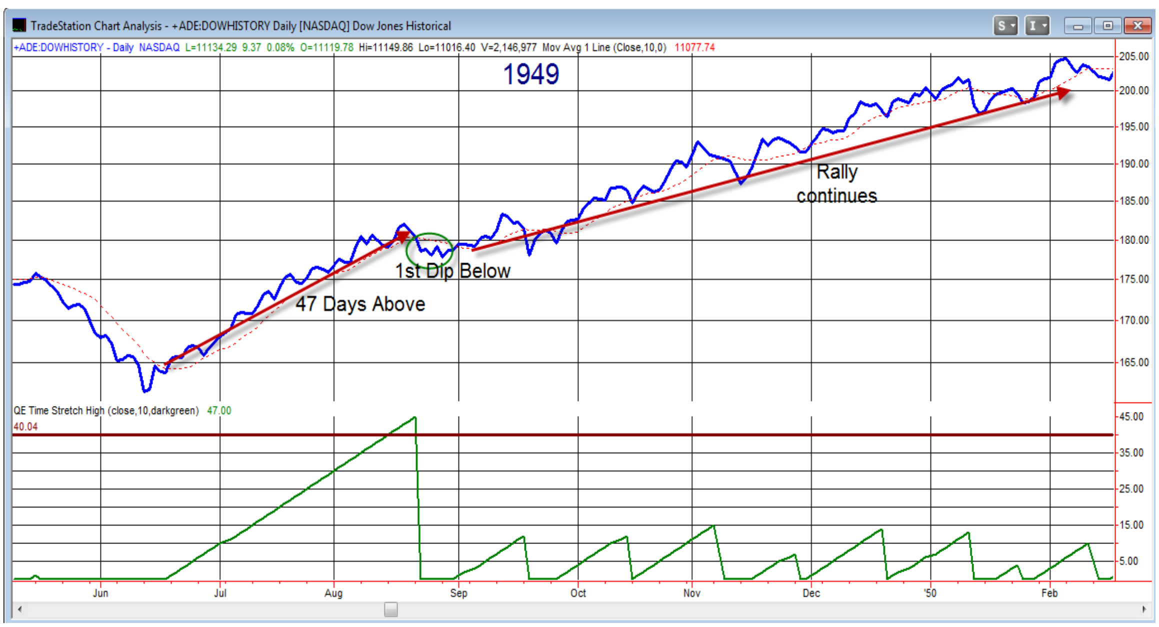
The Dow streak of 48 days is also remarkable. For the Dow Index I was able to look back to 1915 in search of similar streaks. I produced a graphic like the NDX one above, but as you can imagine with history going back that far it was imperceptible. I therefore produced some charts to show the action around similar streaks. There have only been 3 that have lasted as long as the current one. They were in 1919, 1955, and 1971. Their charts are below. The indicator on the bottom is simply a count of the number of days the Dow spent above the 10ma.

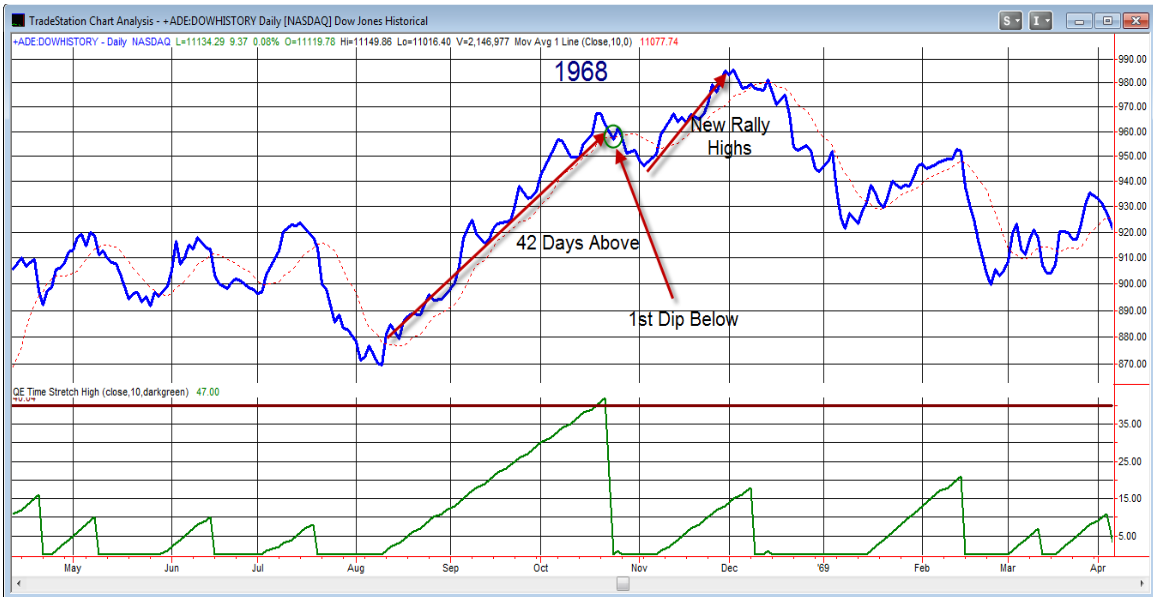




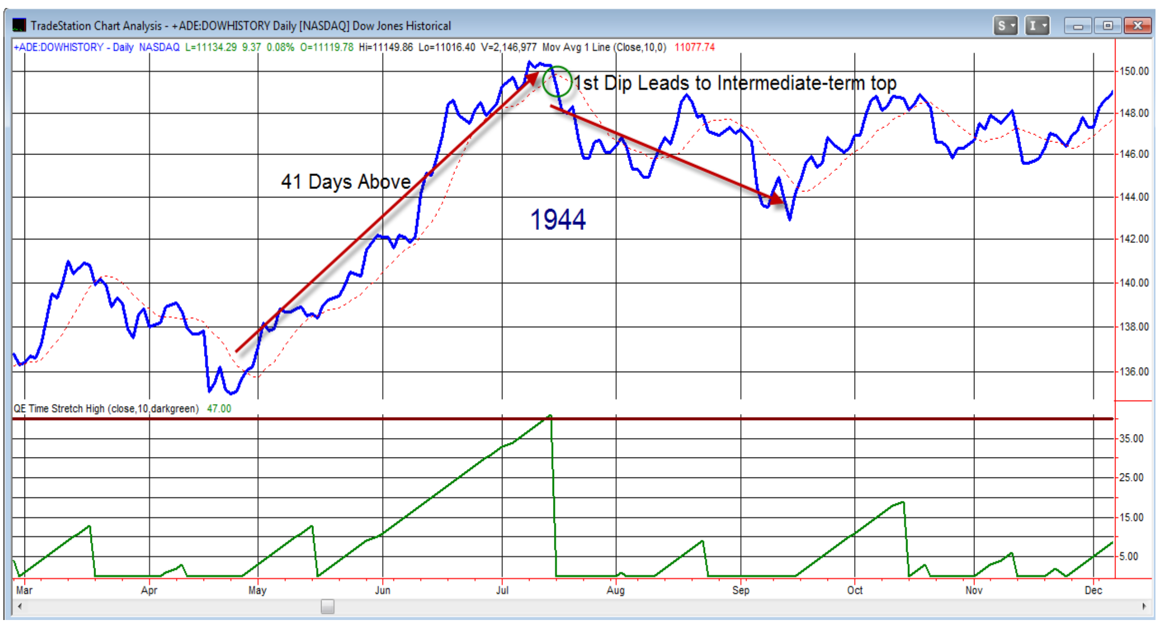


As with the SPX observations we see here that the rally continued in each case after that 1st dip. Rallies this strong and persistent seem unlikely to end on the 1st pullback. In 1949 and 1968 there were rallies that almost reached the current length. I've posted those below.



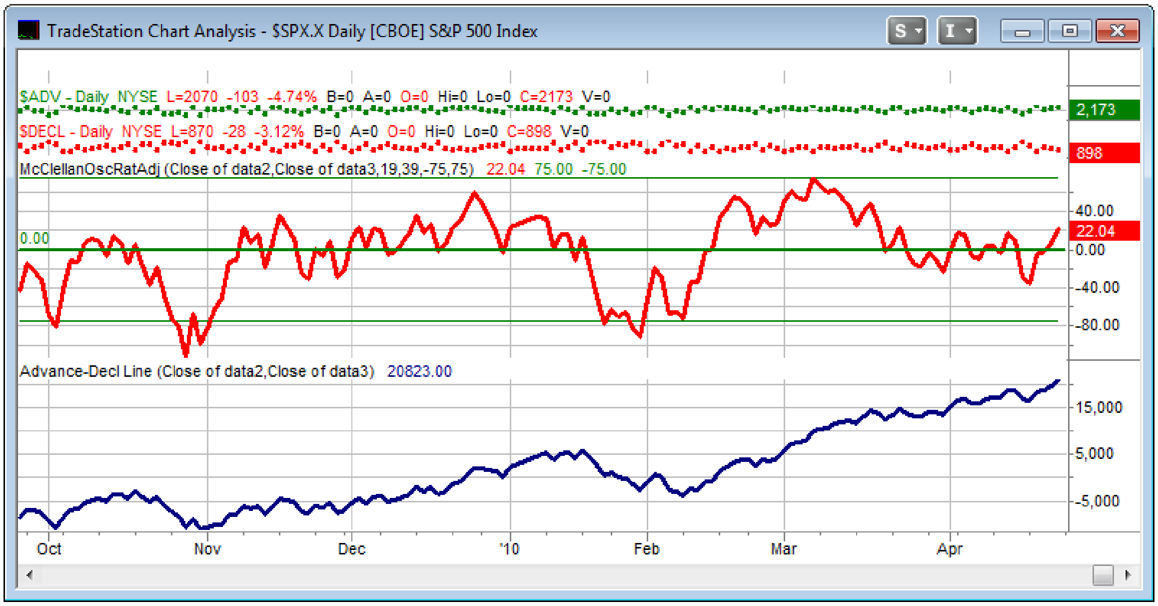


I did look to find the longest streak that ended with the first dip marking an intermediate-term top. 1944 was the winner with a streak of 41 days. That chart is below.



So 1944 could be considered our lone exception as a long streak ended abruptly. Of course it wasn't as long as the current rally or any of those others that went on to further gains.

Another bit of evidence to keep an eye on is the % of 52-week highs on the NYSE. As I've discussed a number of times over the last six months, all SPX tops since 1970 have seen a divergence lasting at least 2 months in either the A/D line or the % of stocks hitting new 52-week highs prior to the ultimate price high. A move higher early this week has the potential to see the 52-week NH % hit a new high. Below is a chart with the NYSE A/D line shown in blue in the bottom panel.



There are a few intermediate-term studies active with bearish implications. They are related to bond action and option ratios. To this point they haven't made a difference. We will get an intermediate-term decline at some point here but for now evidence appears to favor continued upside. It's been a tough trend to fight and I wouldn't suggest it at this point.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Triggers

MON 1/3 position @ $64.73 limit (not filled)

New

QCOM – buy 1/3 position @ $37.92 limit

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 2 (MON, QCOM)

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 @ $118.48. I'll continue to scale in based on the Aggregator and the short-term outlook above.

QCOM – buy 1/3 position @ $37.92 limit. Based on the new Catapult trigger above.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Pri	% Gain/Los	Stop	Notes
SPY(1/4)	4/27/2010	$118.48	$118.48	0.00%		bought on close
SPY(1/4)	4/27/2010	$118.48	$118.48	0.00%		sell @ 2pm

I'll be looking to exit the lot that was based on a Fed Day trade prior to the announcement tomorrow. Should the market start the day strong I may trail a stop as we approach 2pm.