

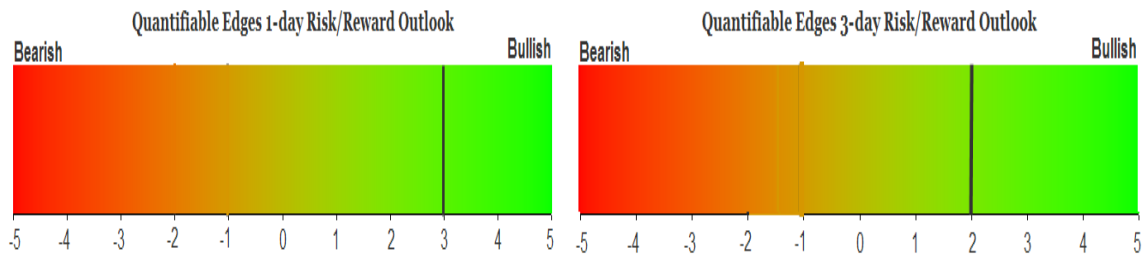
# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 14, 2010

Volume 3 Issue 92

## Market Overview



## Tonight's Research Points

- Outside days down that started with a gap down like today have historically led to a short-term bounce.
- The Aggregator System went long at the close.
- The NDX Aggressive Trend Timer remained flat at the close.

## *Short-term Outlook – updated 5/14*

### *The Bottom Line*

Expectations have now swung back positive. The situation does remain tenuous and volatile, though. I'm looking to slowly scale in to a long index position.

*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
<b>Active</b>				
May 14, 2010	Gap lower then outside day down	1-4 days	Bullish	2.10%
May 6, 2010	Gap & partial reverse from 5-day low	1-10 days	Bullish	3.30%
<b>Active - Long Term</b>				
May 13, 2010	2 of 3 75% Up Issues. No 10-high.	1-2 weeks	<b>Bearish</b>	
April 26, 2010	No breadth divergence at new high	int. term	Bullish	

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

### ***The Evidence***

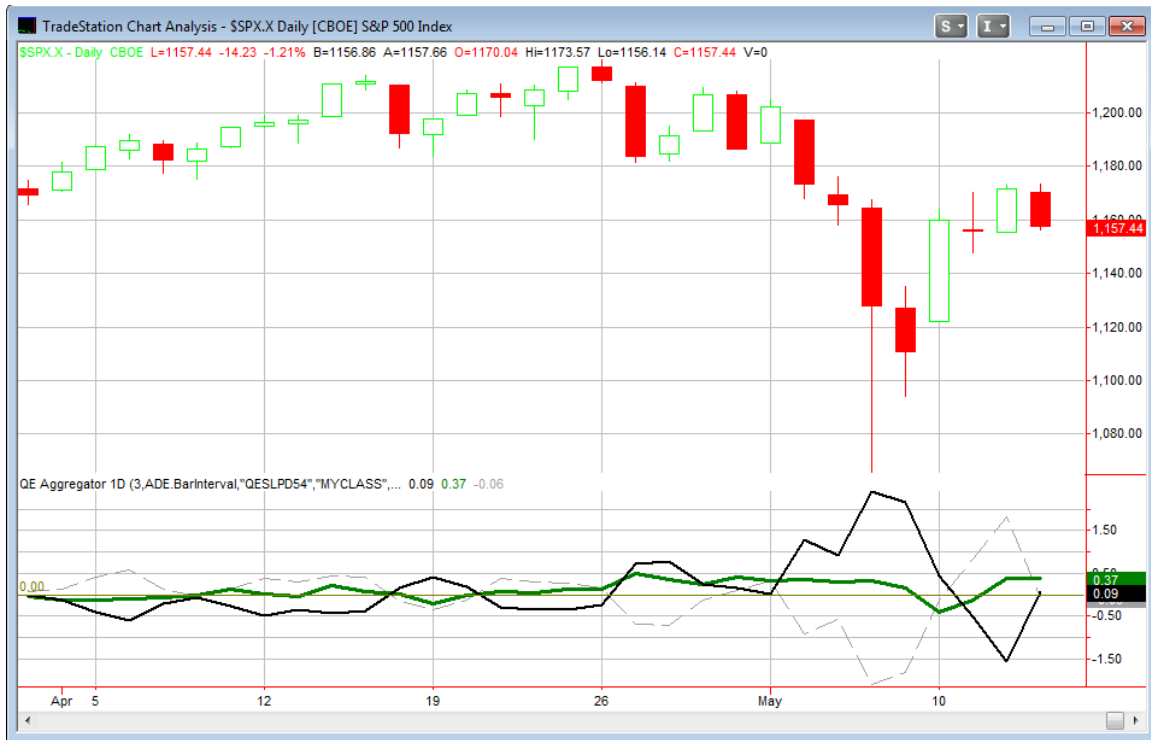
The selling came a day later than we expected. Thursday started with a morning gap down. That gap did fill for the S&P but it couldn't muster much beyond that. A little after 2pm the strong selling arrived. The market went from flat to down substantially. The SPX lost 1.2%, the Nasdaq 1.3% and the Russell 2000 dropped 0.9%. Breadth was solidly negative as the NYSE Up Issues % came in at 34% and the Up Volume % was 22%. Total volume picked up a little during the late selling but still finished lower for the 5<sup>th</sup> straight day.

I examined Thursday's price pattern a number of different ways and continually saw evidence suggesting short-term bullish implications. I've found some outside day down patterns to be bullish in the past and while the big red bar may appear bearish to some, history tells a different story. Below is one example of the kind of compelling evidence I saw when looking at patterns like Thursday.

<b>SPY gaps down, rises to make a higher high then falls and closes below yesterday's low.            Buy on close. Sell X days later. \$100k/trade. 1994 - present.</b>										
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	37,826.14	25	17	8	68.00	3,252.21	-2,182.68	1.49	3.17	1,513.05
9	35,130.11	25	17	8	68.00	3,004.49	-1,993.29	1.51	3.20	1,405.20
8	24,479.69	25	17	8	68.00	2,596.97	-2,458.61	1.06	2.24	979.19
7	20,021.29	25	16	9	64.00	2,606.55	-2,409.27	1.08	1.92	800.85
6	32,018.87	25	17	8	68.00	2,559.89	-1,437.41	1.78	3.78	1,280.75
5	21,864.65	26	19	7	73.08	1,927.74	-2,108.93	0.91	2.48	840.95
4	26,720.64	26	19	7	73.08	1,979.90	-1,556.79	1.27	3.45	1,027.72
3	21,389.85	26	19	7	73.08	1,584.40	-1,244.83	1.27	3.45	822.69
2	10,711.39	26	17	9	65.38	1,305.59	-1,275.95	1.02	1.93	411.98
1	7,049.94	26	19	7	73.08	877.92	-1,375.79	0.64	1.73	271.15
<b>25 of 26 instances (96%) closed above the entry price at            some point in the next 5 days.</b>										

Across the board the numbers appear solidly bullish. They are even a bit more bullish when including filters like "no 10-day high" or "close > 200ma". I elected to use this study though because the number of instances was more substantial this way and the extra filters didn't make a big difference.

I've updated the [Aggregator](#) chart below.



Tonight's bullish study has helped keep the green Aggregator line solidly above zero. This illustrates the net expectation from the Active Studies List is for upside over the next few days. Meanwhile the back Differential line edged slightly positive as the selloff was just enough to put the market in a state where the SPX has now underperformed expectations over the last few days. Positive expectations along with recent underperformance means both lines are above zero. Historically this configuration has provided an upside edge. It caused the Aggregator System to go long at the close on Thursday.

Looking ahead the green Aggregator line is set up to remain positive unless some very compelling bearish evidence arrives. Meanwhile the Differential pivot value on Friday will be 1,151.36. In other words any close at or above this level will drop the Differential line back below 0. So for the Differential to remain positive and the long signal to remain active as of Friday's close the SPX would need to sell off a little over 0.5%.

While the inclinations appear bullish we are now in a highly volatile market and there is plenty of room to the downside on the chart. I normally try and get 2 (of 4) lots on the first day I enter an Aggregator trade and then scale in a little more after that. Because of the high volatility and the relatively high price level compared to a few days ago I'm not

inclined to Aggressively trade this one. Like I did a couple of days ago I will test the waters with a small 1-lot trade instead. Details in the trade idea section below.

***Intermediate-term Outlook (2 weeks – 2 months)– updated 5/10 neutral***

I actually discussed most of the intermediate-term implications in the short-term section above, so I don't have a lot more to add here tonight. One notable is that Nasdaq/S&P Relative Strength indicator which is tracked on the charts page, flipped this week so that the S&P is now leading for the 1<sup>st</sup> time in a few months. This isn't necessarily bearish, but rather a neutral position.

There were also 2 bearish studies that were eliminated from the active list on Thursday night as they met their targets with the big selloff Thursday.

As shown above, breadth and price action are suggesting new highs. Meanwhile the VIX stretch charts seen above are suggesting a bit of a consolidation is likely. In any case, judging the intermediate-term is more difficult when the short-term is so in flux. I'll be watching the bounce closely this week and evaluating further based on the implications suggested by the bounce.

**Catapult and Capitulative Breadth Statistics**

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

***Open Catapult Triggers***

*MON - 1/3 position @ \$64.73 limit ( filled @ \$62.60)*

*MON – 1/3 position @ \$62.25 limit (filled @ \$60.74)*

*MON – 1/3 position @ \$55.54*

***Catapult for ETF's Trades***

*None*

***Broad Market Large Cap CBI – 3 (MON-3)***

### **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 @ \$115.99 LIMIT. If not filled in 1<sup>st</sup> ½ hour, cancel order and place as \$115.40 Limit ON CLOSE order. This is based on the short-term outlook and the Aggregator configuration.*

*MON – buy final 1/3 position @ \$55.54 limit. The third Catapult trigger arrived in this trade that has been quite negative so far. This is the last possible entry.*

### **Active Trades Table**

<b>Symbol</b>	<b>Entry Date</b>	<b>Entry Price</b>	<b>Current Pri</b>	<b>% Gain/Los</b>	<b>Stop</b>	<b>Notes</b>
MON(1/3)	4/29/2010	\$62.60	\$55.54	-11.28%		Catapult
MON(1/3)	5/5/2010	\$60.74	\$55.54	-8.56%		Catapult

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