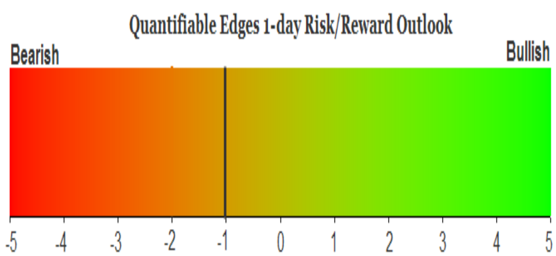
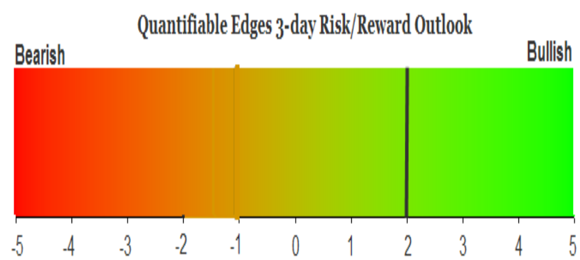
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 18, 2010 Volume 3 Issue 94

Market Overview





Tonight's Research Points

- The slight up close means a weak bounce appears to be in the works.
- The most bearish studies tonight involve looking at the poor breadth numbers.
- The Aggregator System remained long at the close.
- The NDX Aggressive Trend Timer remained long.

***Short-term Outlook** – updated 5/18*

The Bottom Line

The weak bounce today could mean a quick roll over. The Aggregator remained positive by the skin of its teeth even though the studies have a downside expectation for tomorrow.

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				
May 18, 2010	Bad Breadth Bounce Studies	1-2 days	Bearish	-2.30%
May 17, 2010	5% Up Vol. SPX >200ma or >10day low	1-3 days	Bullish	3.80%
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%
Active - Long Term				
May 17, 2010	Nasdaq/SPX Relative Strength Indicator	int. term	Bullish	
May 13, 2010	2 of 3 75% Up Issues. No 10-high.	1-2 weeks	Bearish	
April 26, 2010	No breadth divergence at new high	int. term	Bullish	
Dropped Tonight				
May 17, 2010	Down Friday	1 day	Bullish	

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

The Evidence

The streak of up Mondays following down Fridays continued, but only with a surge in the last 15 minutes. After being down close to 2% just after noon, the SPX fought its way back to finish positive. At the close the SPX had gained 0.1% and the Nasdaq and Russell were up about 0.3%. Breadth was notably weak as the NYSE Up Issues % came in at 40.5% and the Up Volume % at 42%. Total volume declined on both the NYSE and the Nasdaq.

The intraday Quantifinder was filled with green bullish studies about ½ hour before the close. But when the SPX turned positive on the day with about 15 minutes left in the day, those green studies were replaced with red bearish ones. I examined some of the more compelling ones tonight.

First, below is an excerpt from the 6/18/2009 Subscriber Letter. It compared slight down closes to slight up closes after the market had already dropped for 2 days. (*Note: the results in these studies have not been updated*.)

I decided to run a study on low-magnitude moves to illustrate… First I looked at small rises after 2 days down.

SPX closes up today after closing down the previous 2. Today's rise is less than 0.2%.
Buy on close. Sell X days later. $100k/trade. 1988 - present.

QE Lowr Clos SpikDn: daysin	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	11,765.28	57	32	25	56.14	1,546.09	-1,508.38	1.02	1.31	206.41
4	-4,290.32	57	28	29	49.12	1,319.87	-1,422.30	0.93	0.90	-75.27
3	-6,919.40	59	27	32	45.76	1,208.21	-1,235.66	0.98	0.83	-117.28
2	-5,082.11	59	30	29	50.85	896.34	-1,102.50	0.81	0.84	-86.14
1	-6,457.80	59	29	30	49.15	517.35	-715.36	0.72	0.70	-109.45

Results over the 1st 4 days are generally bearish.

I then looked at days where the 3rd day was down very slight.

SPX closes down for the 3rd day in a row. Today's drop is less than 0.2%.
Buy on close. Sell X days later. $100k/trade. 1988 - present.

QE Lowr Clos SpikDn: daysin	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	25,257.92	53	32	21	60.38	1,712.94	-1,407.43	1.22	1.85	476.56
4	21,226.50	53	31	22	58.49	1,671.43	-1,390.36	1.20	1.69	400.50
3	11,020.31	53	35	18	66.04	1,271.73	-1,860.57	0.68	1.33	207.93
2	17,648.58	53	33	20	62.26	1,241.11	-1,165.40	1.06	1.76	332.99
1	14,849.73	53	36	17	67.92	791.92	-803.48	0.99	2.09	280.18

Results across the board are much stronger here. Nearly every column is an improvement over the previous test. I also decided to run the tests from 1999-present.

SPX closes up today after closing down the previous 2. Today's rise is less than 0.2%.
Buy on close. Sell X days later. $100k/trade. 1999 - present.

QE Lowr Clos SpikDn: daysin	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	1,680.00	23	11	12	47.83	2,077.06	-1,763.97	1.18	1.08	73.04
4	-10,128.99	23	10	13	43.48	1,631.55	-2,034.19	0.80	0.62	-440.39
3	-7,353.22	23	9	14	39.13	1,697.46	-1,616.45	1.05	0.68	-319.71
2	-6,622.90	23	10	13	43.48	1,230.59	-1,456.06	0.85	0.65	-287.95
1	-8,663.35	23	9	14	39.13	674.69	-1,052.54	0.64	0.41	-376.67

SPX closes down for the 3rd day in a row. Today's drop is less than 0.2%.
Buy on close. Sell X days later. $100k/trade. 1999 - present.

QE Lowr Clos SpikDn: daysin	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	11,453.00	23	11	12	47.83	2,675.84	-1,498.44	1.79	1.64	497.96
4	11,604.63	23	12	11	52.17	2,384.41	-1,546.21	1.54	1.68	504.55
3	-108.95	23	13	10	56.52	1,810.31	-2,364.30	0.77	1.00	-4.74
2	9,905.76	23	15	8	65.22	1,594.57	-1,751.60	0.91	1.71	430.69
1	11,439.34	23	17	6	73.91	991.04	-901.39	1.10	3.12	497.36

As you can see, over the last 10 years the difference has been even more pronounced.

The takeaway here for me is that a slight up close vs. a slight down close does matter. I've looked at consequences of weak bounces many different ways over the years. Some of those studies appeared tonight.

I've shown many times before the study that looks at drops of 1.75% or more one day followed by a bounce the next day that fails to make up at least 25% of the 1st day's drop. In the 3/9/2009 Letter I noted that the downside edge apparent in this setup didn't seem to occur when there was a strong intraday bounce that took the SPX up at least 1.5% above its daily lows. Below I have broken down the setup to look at times the market experienced a strong intraday bounce versus times it didn't. To get a few more instances I looked back to 1982 rather than 1988 like the original test.

First let's look at instances without a strong intraday reversal.

SPX closes down at least 1.75% yesterday. Today it closes higher but makes up less than 25% of yesterday's loss. It finishes less than 1.5% above its low. Buy on close. Sell X days later. $100k/trade. 1982 - 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	-59,615.54	48	15	33	31.25	2,952.09	-3,148.39	0.94	0.43	-1,241.99
9	-57,376.08	49	17	32	34.69	2,365.98	-3,049.93	0.78	0.41	-1,170.94
8	-36,432.75	51	19	32	37.25	2,471.64	-2,606.06	0.95	0.56	-714.37
7	-38,770.57	52	23	29	44.23	2,224.29	-3,101.00	0.72	0.57	-745.59
6	-30,340.72	52	22	30	42.31	2,135.42	-2,577.33	0.83	0.61	-583.48
5	-46,216.64	54	22	32	40.74	1,848.23	-2,714.93	0.68	0.47	-855.86
4	-43,938.29	54	20	34	37.04	1,755.90	-2,325.19	0.76	0.44	-813.67
3	-37,871.99	55	18	37	32.73	1,713.14	-1,856.99	0.92	0.45	-688.58
2	-23,516.91	56	25	31	44.64	1,145.44	-1,682.35	0.68	0.55	-419.94
1	-23,813.13	56	23	33	41.07	720.45	-1,223.74	0.59	0.41	-425.23

These results suggest a downside edge. Now let's look at times like now where an intraday reversal did occur.

SPX closes down at least 1.75% yesterday. Today it closes higher but makes up less than 25% of yesterday's loss. It finishes at least 1.5% above its low. Buy on close. Sell X days later. $100k/trade. 1982 - 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	40,194.07	18	14	4	77.78	3,807.98	-3,279.41	1.16	4.06	2,233.00
9	47,686.48	18	14	4	77.78	4,336.79	-3,257.16	1.33	4.66	2,649.25
8	48,243.86	18	14	4	77.78	5,147.12	-5,953.97	0.86	3.03	2,680.21
7	34,133.04	18	12	6	66.67	4,494.55	-3,300.27	1.36	2.72	1,896.28
6	22,704.44	18	10	8	55.56	3,958.59	-2,110.19	1.88	2.34	1,261.36
5	26,673.37	18	13	5	72.22	2,698.34	-1,681.01	1.61	4.17	1,481.85
4	16,822.87	18	11	7	61.11	2,755.29	-1,926.48	1.43	2.25	934.60
3	16,505.28	18	10	8	55.56	2,983.90	-1,666.71	1.79	2.24	916.96
2	7,340.23	18	10	8	55.56	2,481.79	-2,184.71	1.14	1.42	407.79
1	8,648.42	18	10	8	55.56	1,718.08	-1,066.55	1.61	2.01	480.47

Here it appears that not only is the downside edge eliminated, but it is actually reversed. We now see a possible upside edge based on these 18 instances.

Another study that appeared in the Quantifinder tonight was from the 2/8/10 Letter. It looked at bounces with weak breadth following a sizable drop. I've updated the results below.

Yesterday SPX drops > 1.5%. Today SPX closes higher but Up Issue % < 45%. Buy on close. Sell X days later. $100k/trade. 2000 - 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	-18,385.83	21	6	15	28.57	3,911.45	-2,790.30	1.40	0.56	-875.52
4	-19,512.07	21	5	16	23.81	3,409.89	-2,285.10	1.49	0.47	-929.15
3	-24,196.61	21	6	15	28.57	2,660.41	-2,677.27	0.99	0.40	-1,152.22
2	-31,591.65	21	7	14	33.33	1,681.58	-3,097.33	0.54	0.27	-1,504.36
1	-25,868.65	21	4	17	19.05	2,043.03	-2,002.40	1.02	0.24	-1,231.84

19 of 21 instances (90%) closed below the entry price at some point in the next 3 days.

These results are suggestive of a downside edge. I thought here it might be interesting to apply the same reversal filter that changed the look of the previous study. Below I did just that.

Yesterday SPX drops > 1.5%. Today SPX closes higher but Up Issue % < 45%. SPX closes at least 1.5% above its lows. Buy on close. Sell X days later. $100k/trade. 2000 - 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	-7,033.50	13	4	9	30.77	5,501.02	-3,226.40	1.71	0.76	-541.04
4	-8,054.96	13	4	9	30.77	3,852.35	-2,607.15	1.48	0.66	-619.61
3	-12,523.88	13	5	8	38.46	3,007.41	-3,445.11	0.87	0.55	-963.38
2	-22,559.73	13	4	9	30.77	2,480.88	-3,609.25	0.69	0.31	-1,735.36
1	-19,846.49	13	2	11	15.38	3,243.50	-2,393.95	1.35	0.25	-1,526.65

12 of 13 instances (92%) closed below the entry price at some point in the next 3 days.

In this case there was no deterioration of the downside edge. This suggests the intraday reversal fails to improve the outlook.

This last study was most recently found in the 12/31/2009 Letter. I have updated the results bwloe.

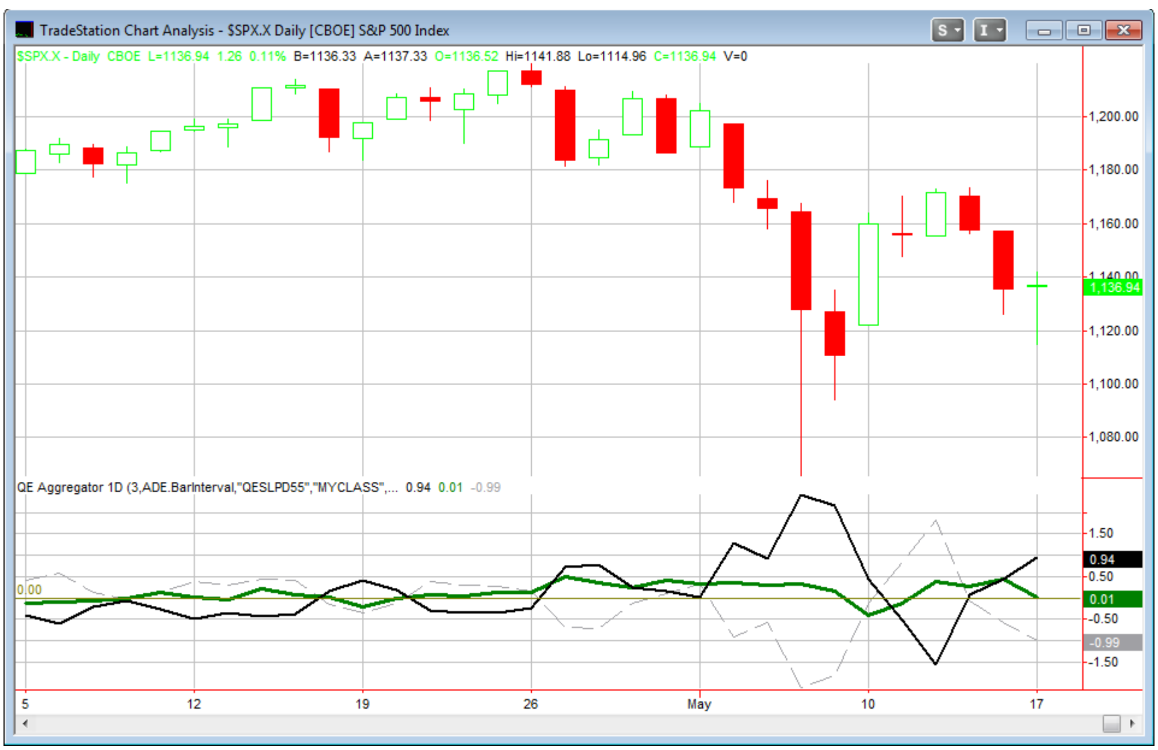
SPX rises while NYSE Up Issue % < 45% and Up Volume % < 45%.
Buy on close. Sell X days later. $100k/trade. 2000 - present.

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	-18,015.33	27	10	17	37.04	1,941.81	-2,201.96	0.88	0.52	-667.23
4	-29,401.36	27	9	18	33.33	1,364.87	-2,315.85	0.59	0.29	-1,088.94
3	-33,915.72	28	8	20	28.57	1,317.94	-2,222.96	0.59	0.24	-1,211.28
2	-33,842.03	28	11	17	39.29	955.66	-2,609.07	0.37	0.24	-1,208.64
1	-23,297.66	28	9	19	32.14	879.94	-1,643.01	0.54	0.25	-832.06

24 of 28 instances (86%) closed below the entry price at some point in the next week.

Like the previous study I filtered this one to look at times the market made a 1.5% intraday reversal as well. There were only 6 instances but they didn't suggest an upside edge. I also tested these weak breadth studies to see if long-term trend mattered. The downside edge held up even above the 200ma.

I've updated the Aggregator chart below.



Tonight's bearish studies dropped the green Aggregator line almost to zero. Still it did manage to finish just above, implying an upside edge over the next few days. Not visible in the chart is that expectations for just tomorrow are for downside. Meanwhile the black Differential line remains well above zero. This illustrates the fact that the SPX has strongly underperformed expectations over the last few days. With both lines still above zero the Aggregator configuration remains bullish. The Aggregator System is still long.

Looking ahead the green Aggregator line is set to remain positive tomorrow. The short-term studies are all expiring in just a couple of days, though. That means new studies that emerge in the next couple of days will determine the bias going forward. The Differential pivot value is 1,163. In other words, it would take an SPX close at or above this level in order to flip the Differential line negative.

The studies tonight were predominantly bearish, the Aggregator value was just barely positive, and the 1-day expectations from the studies are actually negative. While the basic Aggregator configuration remains bullish, these reasons all suggest not pressing. I'll wait another day to see how the market unfolds before looking to adjust my exposure.

Intermediate-term Outlook (2 weeks – 2 months)– updated 5/17 neutral

One positive intermediate-term indicator that emerged Friday was the Nasdaq/S&P 500 Relative Strength again began to favor the Nasdaq. I've discussed this indicator several times before, but for those who would like a refresher, below is a link to the original post:

http://quantifiableedges.blogspot.com/2009/05/simple-powerful-timing-indicator.html

The 2 strong up days on Monday and Wednesday last week that occurred without the SPX managing to hit a 10-day high suggest bearish implications. Below is the study from the Wednesday night letter that illustrated this:

NYSE Up Issues % > 75% in 2 of last 3 days. High < highest high of last 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
10	-24,084.16	14	4	10	28.57	2,422.57	-3,377.44	0.72	0.29	-1,720.30
9	-25,100.34	15	6	9	40.00	2,388.07	-4,380.97	0.55	0.36	-1,673.36
8	-22,911.44	15	6	9	40.00	1,909.19	-3,818.51	0.50	0.33	-1,527.43
7	-14,751.96	15	6	9	40.00	2,735.37	-3,462.69	0.79	0.53	-983.46
6	-10,851.43	15	5	10	33.33	2,553.51	-2,361.90	1.08	0.54	-723.43
5	-8,955.02	15	7	8	46.67	1,939.97	-2,816.86	0.69	0.60	-597.00
4	4,662.08	15	10	5	66.67	1,517.92	-2,103.42	0.72	1.44	310.81
3	5,531.01	15	9	6	60.00	2,254.85	-2,460.44	0.92	1.37	368.73
2	786.94	16	10	6	62.50	1,430.05	-2,252.25	0.63	1.06	49.18
1	10,166.79	17	10	7	58.82	1,312.77	-422.99	3.10	4.43	598.05

Bottom line right now is that risk is elevated and intermediate-term signals are mixed. There is a high amount of uncertainty and although a bounce appears likely, what's beyond that is unclear. Using a bit extra caution when considering risk management and also looking to the short-term analysis to aide more in guiding decisions are two steps traders may want to consider.

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 limit (filled @ $54.79)

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.

NONE tonight.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Pri	% Gain/Los	Stop	Notes
MON(1/3)	4/29/2010	$62.60	$55.48	-11.37%		Catapult
MON(1/3)	5/5/2010	$60.74	$55.48	-8.66%		Catapult
MON(1/3)	5/14/2010	$54.79	$55.48	1.26%		Catapult
SPY(1/4)	5/14/2010	$115.12	$113.95	-1.02%		Aggregator

The SPY trade idea from yesterday did not fill. Should we move lower and trigger some bullish studies, I'll probably be looking to buy more in tomorrow's Letter.