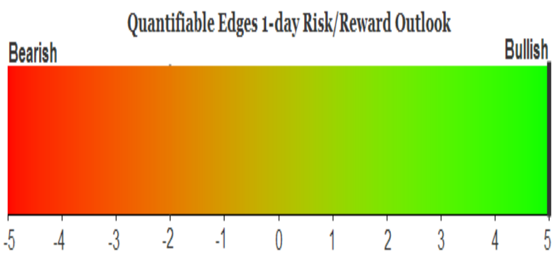
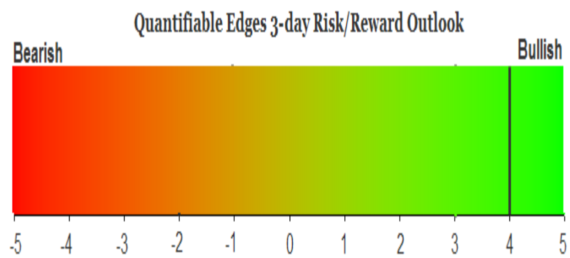
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 16, 2010 Volume 3 Issue 221

Market Overview





Tonight's Research Points

- 3 Down days with today being Monday suggests an upside edge.
- The slowing momentum in the decline also suggests it should bounce soon.
- The Aggregator System is long.
- The NDX Aggressive Trend Timer is long.

Short-term Outlook

The Bottom Line

More bullish evidence is emerging and the SPX is still very oversold. I am anticipating a bounce and positioning myself to 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
Active				
November 16, 2010	SPX down 3 on a Monday	1-5 days	Bullish	2.70%
November 16, 2010	SPX down 3. Mildest drop. Vol 5 low.	1-2 days	Bullish	1.70%
November 15, 2010	SPX down 1% Decliners 2x Advancers	1-9 days	Bullish	3.00%
November 15, 2010	SPY 2 unfilled down gaps & 5-day low	1-5 days	Bullish	1.90%
November 15, 2010	SPX down 1% SOX Up	1-6 days	Bullish	2.90%
November 9, 2010	SPX 5+ up days then 1 down	1-6 days	Bullish	2.10%
Active - Long Term				
November 15, 2010	QQQQ 5 lower lows and large drop	1-20 days	Bullish	
November 15, 2010	SPX down 1% SOX Up	1-20 days	Bullish	
November 5, 2010	Very strong breadth & 50-day high	1-30 days	Bullish	
October 25, 2010	SPX Golden Cross	int term	Bullish	
October 18, 2010	SPX up. Issue% and Vol% very low	1-25 days	Bearish	
September 20, 2010	Nas/SPX RS favors Nasdaq	int term	Bullish	
Dropped Tonight				
November 15, 2010	Volume SPYX > 110 and SPX down	1 day	Bullish	
November 15, 2010	Down Friday	1 day	Bullish	
November 8, 2010	%b > 1.15 2 days in row. 20-day high	1-6 days	Bullish	2.20%

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

The Evidence

Despite a boatload of bullish evidence and a strong start to the day with a nice gap up the market could not follow through. Instead it lingered above breakeven for most of the day before a late afternoon selloff saw it end mixed. The SPX lost 0.1% and the Nasdaq fell 0.2% while the Russell 2000 finished up 0.1%. Breadth was a little negative as the NYSE Up Issues % came in at 47% and the Up Volume % was 49%. Total NYSE volume came in at the lowest level in over 3 weeks.

Inside days during a long-term downtrend are often a bad sign. In an uptrend they aren't terribly predictive and don't suggest a bearish edge. I continued to look for possible bearish evidence tonight and again everything compelling is suggesting a bounce. I've updated a couple of the most compelling studies below.

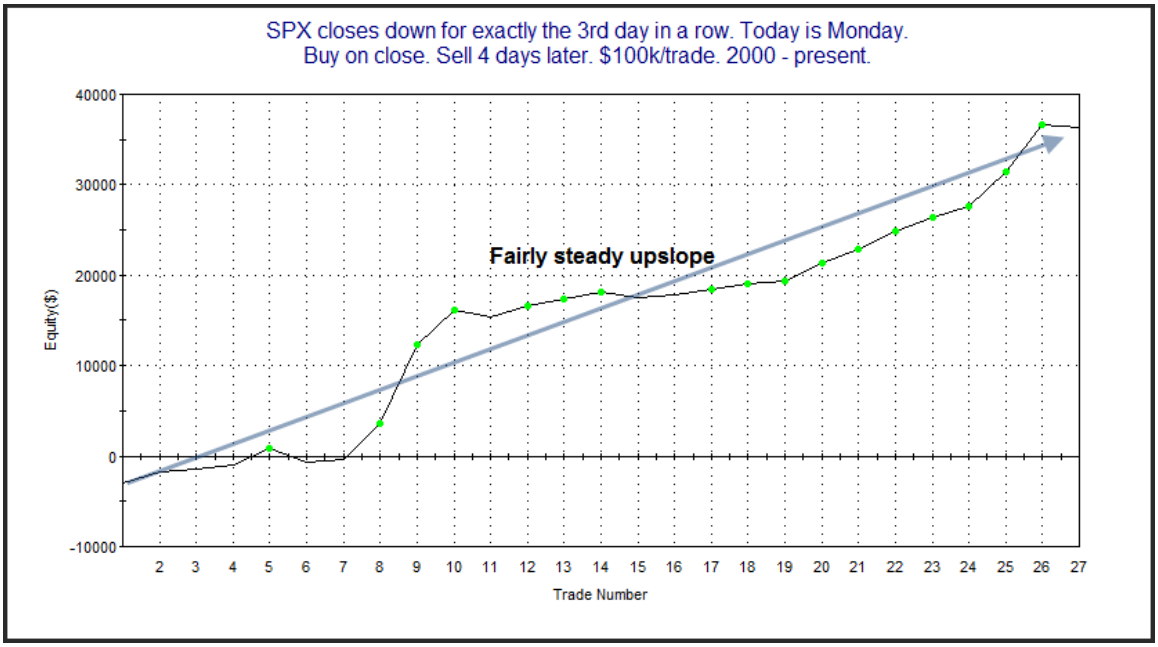
This first one was last seen in the 8/24/10 subscriber letter. I looked at 3-day pullbacks on Mondays. I've shown before that of all days Tuesday has historically shown the highest propensity to halt a short-term pullback. The study below is one from the larger Turnaround Tuesday study.

SPX closes down for exactly the 3rd day in a row. Today is Monday.
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
10	55,602.78	26	21	5	80.77	3,078.81	-1,810.44	1.70	7.14	2,138.57
9	60,383.17	26	21	5	80.77	3,071.90	-825.34	3.72	15.63	2,322.43
8	56,625.89	26	21	4	80.77	2,939.44	-1,275.58	2.30	12.10	2,177.92
7	51,298.49	26	21	5	80.77	2,733.40	-1,220.59	2.24	9.41	1,973.02
6	42,816.76	26	20	6	76.92	2,376.15	-784.39	3.03	10.10	1,646.80
5	46,852.01	27	19	8	70.37	2,763.71	-707.31	3.91	9.28	1,735.26
4	36,339.82	27	22	5	81.48	1,933.55	-1,239.65	1.56	6.86	1,345.92
3	33,305.67	27	20	7	74.07	1,954.26	-825.65	2.37	6.76	1,233.54
2	27,505.88	27	22	5	81.48	1,402.79	-671.11	2.09	9.20	1,018.74
1	16,284.87	27	19	8	70.37	1,169.98	-743.09	1.57	3.74	603.14

25 of 27 instances (93%) closed above the entry price at some point in the next week. All 27 did within 7 trading days.

As you can see the market has strongly favored a quick move higher. And when that move hasn't happened on Tuesday it has often happened in the next few days. Below is an equity curve showing a 4-day exit strategy.



While the strength of the edge has oscillated some it has provided fairly consistent results over time. Certainly this study seems to suggest an upside edge.

In the 9/28/09 Letter I showed that pullbacks that seem to be losing their downside momentum typically provided an upside edge. I used the mild percent change and the lower volume to indicate a momentum loss. Below I have updated that study.

SPX posts at least 3 lower closes. Today is the mildest drop of the decline and the lowest volume in 5 days. Buy 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
10	33,943.18	29	23	6	79.31	2,443.67	-3,710.20	0.66	2.52	1,170.45
9	35,780.58	29	22	7	75.86	2,612.54	-3,099.31	0.84	2.65	1,233.81
8	27,574.60	29	20	9	68.97	2,508.67	-2,510.98	1.00	2.22	950.85
7	27,230.82	29	18	11	62.07	2,650.17	-1,861.11	1.42	2.33	938.99
6	27,433.86	29	17	12	58.62	2,578.53	-1,366.76	1.89	2.67	946.00
5	26,669.88	29	16	13	55.17	2,473.67	-992.99	2.49	3.07	919.65
4	15,154.29	29	15	14	51.72	1,928.33	-983.61	1.96	2.10	522.56
3	16,803.39	29	19	10	65.52	1,633.22	-1,422.77	1.15	2.18	579.43
2	23,614.28	29	22	7	75.86	1,347.39	-861.17	1.56	4.92	814.29
1	16,164.17	29	21	7	72.41	876.31	-319.77	2.74	8.22	557.39

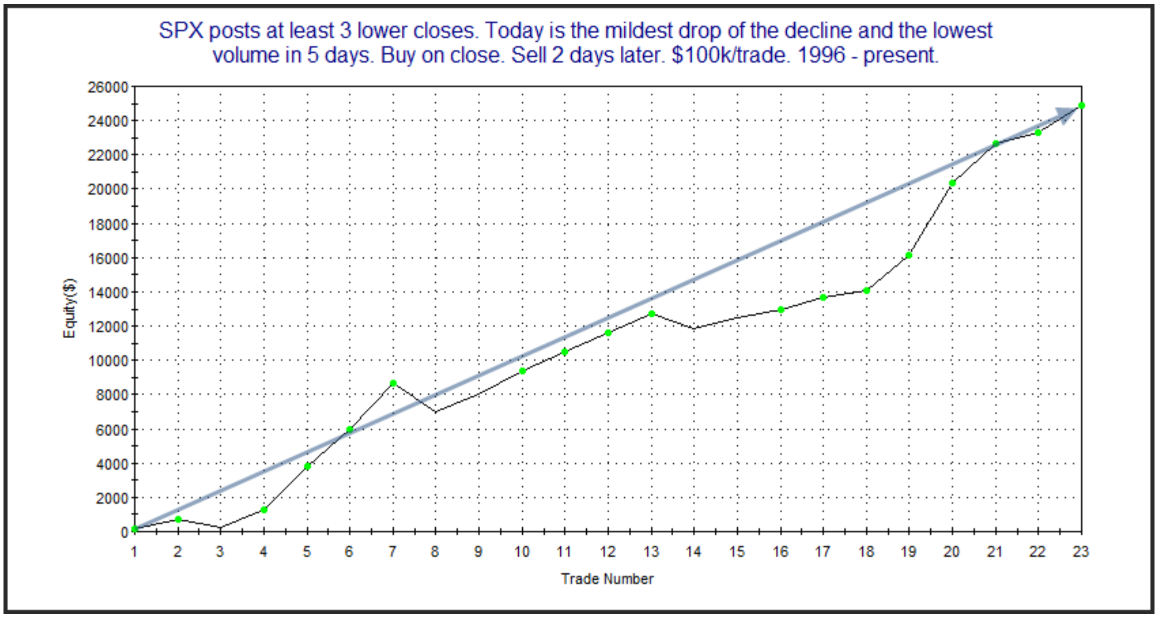
In looking at the equity curve tonight I noted that this study really began to show an upside edge around 1996. Therefore I re-ran results over this slightly shorter time period.

SPX posts at least 3 lower closes. Today is the mildest drop of the decline and the lowest volume in 5 days. Buy on close. Sell X days later. $100k/trade. 1996 - 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	32,846.96	23	19	4	82.61	2,734.44	-4,776.87	0.57	2.72	1,428.13
9	33,806.82	23	18	5	78.26	2,914.92	-3,732.33	0.78	2.81	1,469.86
8	27,200.02	23	16	7	69.57	2,880.70	-2,698.74	1.07	2.44	1,182.61
7	25,611.46	23	13	10	56.52	3,388.35	-1,843.70	1.84	2.39	1,113.54
6	23,760.37	23	12	11	52.17	3,234.67	-1,368.69	2.36	2.58	1,033.06
5	24,840.62	23	12	11	52.17	2,951.18	-961.23	3.07	3.35	1,080.03
4	16,061.05	23	12	11	52.17	2,194.52	-933.93	2.35	2.56	698.31
3	20,180.69	23	18	5	78.26	1,654.25	-1,919.17	0.86	3.10	877.42
2	24,847.38	23	20	3	86.96	1,394.90	-1,016.89	1.37	9.14	1,080.32
1	14,800.32	23	17	5	73.91	981.36	-376.56	2.61	8.86	643.49

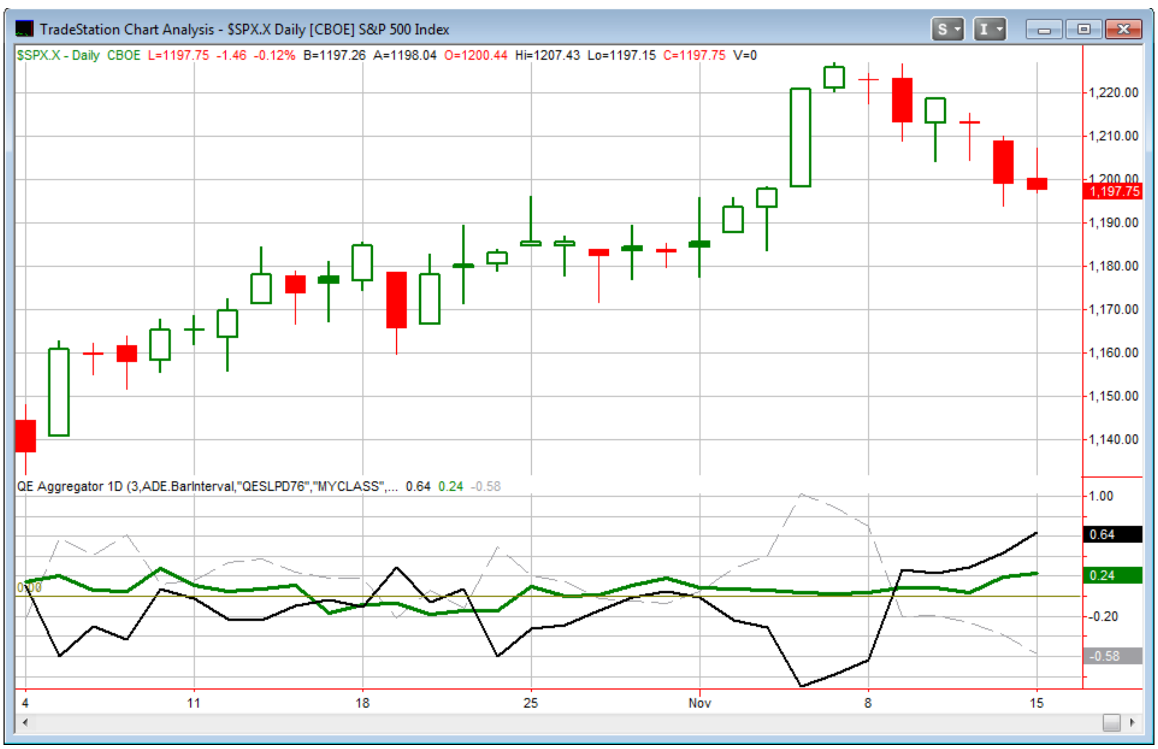
22 of 23 instances (96%) closed above the entry price at some point in the next 4 days.

The edge here appears to be substantial even though much of it is realized within 2 days. In the past I found that this edge appears to be stronger in cases where the decline is coming from at least a 20-day high. I didn't feel it was worth making that distinction tonight. This pullback doesn't count as coming from a 20-day high because of the up day on Wednesday. Still, when looking at the chart most people would say the decline started last Monday and not on Thursday. So I'm not bothering with that type of filter tonight. Below is a profit curve using a 2-day exit strategy.



They don't get much steadier than this one. Although the number of instances is a tad lower than I would prefer, the consistently positive results suggest an upside edge.

I have updated the Aggregator chart below.



The green Aggregator line remained well above zero today. The positive value indicates the net expectation from the Active Studies over the next few days is for a move up. Meanwhile the black Differential line is now farther above 0 than it has been in a long time. The positive value means the SPX has underperformed expectations over the last few days. So we have positive expectations and a market that is strongly oversold. Historically this combination has provided and upside edge. This can be seen on the Aggregator chart whenever both lines are above 0. Due to this the Aggregator System stayed long at the close.

The green Aggregator line is set up to remain positive tomorrow. This is unlikely to change without substantial bearish evidence. Meanwhile, the Differential Pivot will be 1,215.87. Any close at or above this level would move the black Differential line back into negative territory. This means the SPX would need to gain about 1.8% in order to be considered overbought versus expectations.

There is always a chance the short-term decline could accelerate and turn into something worse. Based on historical precedents this appears unlikely. The market is substantially oversold in a long-term uptrend and there is ample evidence suggesting a bounce should be forthcoming. I am looking to take advantage of this bounce. Already with a decent amount of exposure I will be looking to add more tomorrow. You'll find some additional trade ideas in the Trade Idea section below.

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/15 – bullish

Despite the pullback this week there appears to be more bullish intermediate-term evidence emerging and a complete lack of new bearish intermediate-term studies. Both the overdone QQQQ study and the SPX down / SOX up study show a strong propensity for intermediate-term gains.

One possible fly in the ointment is that the recent market high saw a lower number of new highs than the April market high. While not a great timing device, these types of divergences typically exist prior to extended market declines. There have been times in the past though where these divergences have lasted for well over a year before the final top was reached. And of course the divergence still has a chance to right itself. If the market is able to rally to new highs again in the near future and the number of new highs expands beyond April levels then the divergence would no longer exist.

As I've been saying, until the market begins to falter and more bearish evidence emerges I'll continue to trade with a bullish bias. Perhaps it's beginning to falter now but it isn't generating substantial bearish evidence so far. For my own trading a bullish bias means I tend to trade the long side with more aggressiveness and I will be extra selective with short trades.

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

Open Catapult Triggers

GOOG – 1/3 @ $603.29

GOOG – buy 1/3 @ $595.47

Catapult for ETF's Trades

None

***Broad Market Large Cap CBI* – 2 (GOOG)**

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 @ $119.25 LIMIT ON CLOSE. Should the market sell off more on Tuesday I'll look to put on the last piece of my index trade.

GOOG – buy 1/3 position @ $595.47 limit. This is the 2nd of a possible 3 triggers for GOOG. This trade is based on the Catapult System. Those unfamiliar or who would like a review may watch the Catapult & CBI presentation using the link below.

http://www.quantifiableedges.com/videos/QE20100621.html

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	11/10/2010	$121.58	$120.03	-1.27%		Aggregator
AMGN	11/11/2010	$54.28	$54.51	0.42%	$53.90	sell on close>$54.58
SPY(1/4)	11/12/2010	$120.20	$120.03	-0.14%		Aggregator
GD	11/12/2010	$66.50	$66.55	0.08%		System 11111
SPY(1/4)	11/15/2010	$120.20	$120.03	-0.14%		Aggregator
GOOG(1/3)	11/15/2010	$603.00	$595.47	-1.25%		Catapult

AMGN has put in a consolidation and seemed to find support. Should it fail to bounce here we could see another leg down. I don't often use stops on these system trades, but I will sometimes when support forms and the exit trigger has not yet been reached. This is one of those cases. I've place the stop a little below the swing low a couple of days ago.