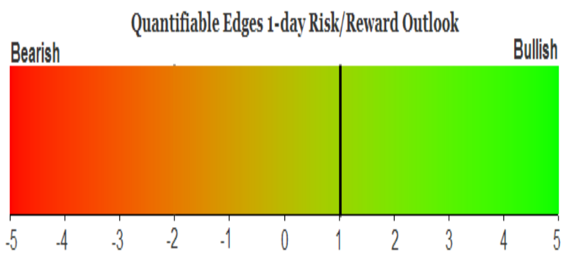
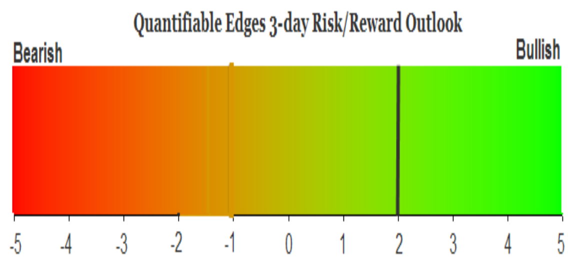
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 24, 2010 Volume 3 Issue 227

Market Overview





Tonight's Research Points

- The low volume on the move up Wednesday favors a pullback.
- The strong reversal in breadth from Tuesday to Wednesday suggests short-term follow through.
- The Aggregator System is long.
- The NDX Aggressive Trend Timer is long.

Short-term Outlook
The Bottom Line

Overall the studies seem to indicate Wednesday's bounce could continue a little further. Should this happen on Friday I'll be looking to take some profits.

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 26, 2010	Lowest vol 20. SPX up 1% in uptrend	1-2 days	Bearish	-1.60%
November 26, 2010	Up Vol % Rank increases > 85%	1-3 days	Bullish	1.30%
November 24, 2010	2 Unfilled Gaps Down in SPY	1-5 days	Bullish	2.10%
November 24, 2010	Wed-Fri Thanksgiving Seasonality	2 days	Bullish	
November 24, 2010	SPX down 1% Decliners 2x Advancers	1-9 days	Bullish	3.00%
November 17, 2010	Down 4 on Wednesday	1-8 days	Bullish	
Active - Long Term				
November 22, 2010	High number of POMO Days recently	int term	Bullish	
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	

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

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The Evidence

Some of the bullish tendencies discussed Tuesday night seemed to kick in on Wednesday. The market opened with a gap up, never pulled back into the gap and closed near its high. The SPX gained 1.5%, the Nasdaq added on 1.9% and the Russell 2000 rose 2.3%. Breadth jumped from extremely negative on Tuesday to extremely positive on Wednesday. The NYSE Up Issues % came in at 82.5% and the Up Volume % was 91%. It appears some traders decided to quit early though as NYSE volume came in at the lowest level in over a month.

The Quantifinder triggered quite a few studies at the end of the day. Many of them were related to the very low volume. Low volume on up days is often a sign of complacency, so it will commonly trigger studies with bearish edges. But Wednesday's volume came one day ahead of Thanksgiving. So perhaps it wasn't so much a sign of complacency, but rather a sign of people taking off early ahead of the holiday. Often when volume comes in extremely light on or just in front of a holiday I will simply dismiss low-volume studies.

Rather than just dismiss them though, I wondered how often does the Wednesday before Thanksgiving post the lowest volume in 20 days. Below is a study that looks at the number of occurrences and the performance following them.

Wednesday before Thanksgiving posts the lowest NYSE volume in 20 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
5	-5,805.85	10	5	5	50.00	1,383.52	-2,544.69	0.54	0.54	-580.59
4	-974.96	10	4	6	40.00	1,687.05	-1,287.19	1.31	0.87	-97.50
3	-5,266.03	10	3	7	30.00	1,647.26	-1,458.26	1.13	0.48	-526.60
2	-10,483.44	10	2	8	20.00	664.12	-1,476.46	0.45	0.11	-1,048.34
1	-2,917.41	10	4	6	40.00	356.81	-724.11	0.49	0.33	-291.74

The 1st instance (1982) was the only one that did not close below Wednesday's close on either Friday or Monday.

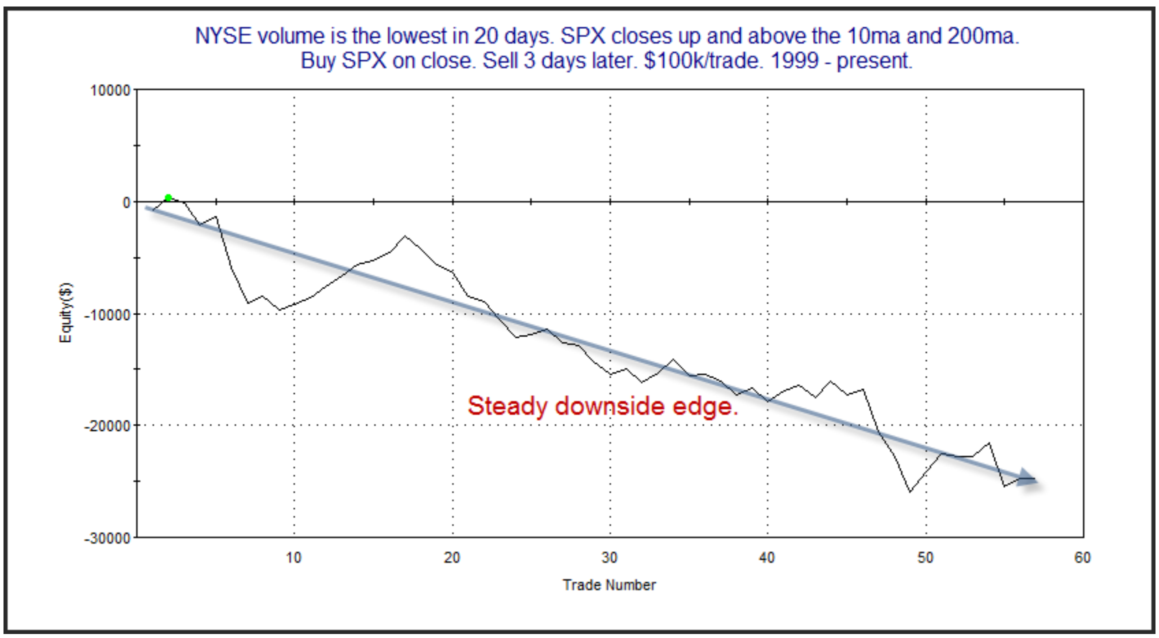
In the last 40 years there have been 10 instances where Wednesday marked a 20-day volume low. This isn't a layup but it's about 4 times higher than you'd get looking at any random day. Interesting is how poorly the SPX has performed over the next 2 days when volume has come in low. The number of instances is low and including these results in the Aggregator would be a questionable decision. It does seem to me though, that with results like this, there doesn't seem to be good reason to discount the other volume studies. So with that in mind I decided to show and consider them in my analysis.

This first one was last seen in the 10/25/10 Subscriber Letter. It looks at very low volume occurring on an up day in an uptrend.

NYSE volume is the lowest in 20 days. SPX closes up and above the 10ma and 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
5	-22,756.72	53	25	28	47.17	1,210.93	-1,893.92	0.64	0.57	-429.37
4	-19,449.00	55	25	30	45.45	903.90	-1,401.55	0.64	0.54	-353.62
3	-24,767.70	57	26	31	45.61	833.94	-1,498.39	0.56	0.47	-434.52
2	-19,434.66	59	23	36	38.98	697.58	-985.53	0.71	0.45	-329.40
1	-8,847.63	64	31	33	48.44	458.37	-698.70	0.66	0.62	-138.24

The results seem to suggest a downside edge over the next few days. Below is an equity curve using a 3-day exit criterion.



There is some choppiness in the returns but the edge has been steady enough for my liking.

I also decided it would be interesting to see how returns looked when the day was not just up, but up at least 1%. Those results are below.

NYSE volume is the lowest in 20 days. SPX closes up over 1% and above to 10ma and 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
5	-4,444.15	9	6	3	66.67	1,409.11	-4,299.60	0.33	0.66	-493.79
4	-5,662.87	9	5	4	55.56	954.84	-2,609.26	0.37	0.46	-629.21
3	-6,366.02	9	4	5	44.44	747.55	-1,871.25	0.40	0.32	-707.34
2	-6,958.02	9	1	8	11.11	1,321.92	-1,034.99	1.28	0.16	-773.11
1	-4,420.32	9	3	6	33.33	480.66	-977.05	0.49	0.25	-491.15

Instances are low but the consistency is compelling. Below I have listed all instances with a 2-day exit.

NYSE volume is the lowest in 20 days. SPX closes up over 1% and above to 10ma and 200ma.Buy SPX on close. Sell 2 days later. $100k/trade. 1999 - present.

Date/Time	Signal	Price	% Profit	Run-up DrawDown
02/16/99	Buy	$1,248.27	(0.88%)	$81.60
02/18/99	Sell	$1,237.28		($2,219.20)
06/30/99	Buy	$1,372.86	1.34%	$1,321.92
07/02/99	Sell	$1,391.22		($871.20)
04/07/00	Buy	$1,516.35	(1.04%)	$704.60
04/11/00	Sell	$1,500.58		($1,918.15)
07/03/00	Buy	$1,469.32	(0.86%)	$14.96
07/06/00	Sell	$1,456.67		($2,023.68)
08/07/00	Buy	$1,479.32	(0.44%)	$740.35
08/09/00	Sell	$1,472.87		($536.00)
08/14/00	Buy	$1,491.54	(0.78%)	$304.85
08/16/00	Sell	$1,479.85		($1,058.60)
04/14/03	Buy	$885.23	(0.60%)	$1,292.48
04/16/03	Sell	$879.91		($817.60)
08/24/07	Buy	$1,479.37	(3.18%)	$0.00
08/28/07	Sell	$1,432.36		($3,173.12)
09/28/09	Buy	$1,062.98	(0.56%)	$595.96
09/30/09	Sell	$1,057.08		($1,551.94)

The 6/30/99 instance did not lead to a pullback and continued to rally for another 3 weeks.

But while volume is suggesting the rally may need a pause or pullback here, breadth was not confirming this view. The 90% upside volume on Wednesday was very strong. Combined with the low volume it triggered a study last shown in the 9/21/10 subscriber letter. I have updated that study below.

NYSE Up Volume % > 90% while NYSE total volume declines. SPX > 200ma.
Buy on close. Sell X days later. $100k/trade. 1970 - presemt.

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	-639.50	10	5	5	50.00	3,281.24	-3,409.14	0.96	0.96	-63.95
9	2,807.62	10	7	3	70.00	2,228.08	-4,262.99	0.52	1.22	280.76
8	-1,079.95	10	5	5	50.00	2,766.26	-2,982.25	0.93	0.93	-108.00
7	1,426.20	10	5	5	50.00	2,325.56	-2,040.32	1.14	1.14	142.62
6	2,367.73	10	4	6	40.00	2,470.53	-1,252.40	1.97	1.32	236.77
5	4,286.01	10	5	5	50.00	1,910.54	-1,053.34	1.81	1.81	428.60
4	6,794.84	10	7	3	70.00	1,575.93	-1,412.22	1.12	2.60	679.48
3	6,259.84	10	5	5	50.00	1,939.66	-687.69	2.82	2.82	625.98
2	7,072.93	10	8	2	80.00	1,022.96	-555.39	1.84	7.37	707.29
1	2,079.51	10	4	6	40.00	1,155.88	-424.00	2.73	1.82	207.95

9 of 10 instances closed above the entry price at some point in the next 4 days.

Like the Wednesday before Thanksgiving volume study we have a low number of instances here. Results are somewhat compelling but it's borderline. I won't be including this study but will continue to keep an eye on it.

Wednesday's 90% up day came right after a 90% down day on Tuesday. Looking back to 1970 I was only able to identify 2 other instances where this occurred while the SPX was above the 200ma.

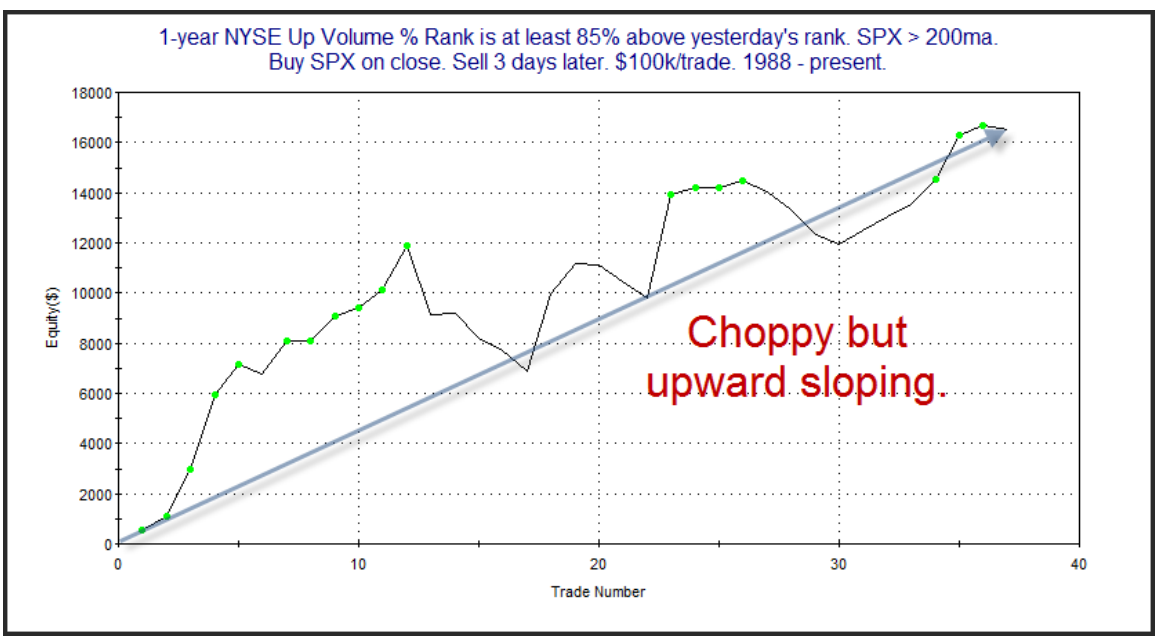
While 2 instances is certainly too low to infer anything from I thought the concept of a strong breadth reversal might be worth considering. As I've mentioned many times in the last several months, 90% volume days have become much more common in the last 2 years than they were at any time prior to that. So rather than using the static 90% requirement I decided to look at the Up Volume % Rank as shown on the charts page. The % Rank on Wednesday was 94% and on Tuesday it was 7% for a difference of 87%. I therefore looked at other times there was an increase of at least 85% in the % Rank from one day to the next while the SPX was in an uptrend. That study is below.

1-year NYSE Up Volume % Rank is at least 85% above yesterday's rank. SPX > 200ma.
Buy SPX on close. Sell X days later. $100k/trade. 1988 - 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	23,283.31	34	24	10	70.59	1,727.68	-1,818.11	0.95	2.28	684.80
9	23,635.64	35	27	8	77.14	1,520.87	-2,178.49	0.70	2.36	675.30
8	3,284.90	35	23	12	65.71	1,284.78	-2,188.75	0.59	1.13	93.85
7	9,278.64	35	19	16	54.29	1,608.92	-1,330.68	1.21	1.44	265.10
6	10,655.38	35	21	14	60.00	1,443.76	-1,404.54	1.03	1.54	304.44
5	5,050.13	35	20	15	57.14	1,456.85	-1,605.80	0.91	1.21	144.29
4	11,145.22	35	20	15	57.14	1,236.90	-906.19	1.36	1.82	318.43
3	16,488.13	37	24	13	64.86	1,084.33	-733.53	1.48	2.73	445.63
2	11,149.42	37	23	14	62.16	1,002.80	-851.07	1.18	1.94	301.34
1	5,439.75	37	19	18	51.35	713.53	-450.96	1.58	1.67	147.02

86% of instances posted a close above the entry price at some point in the next week.

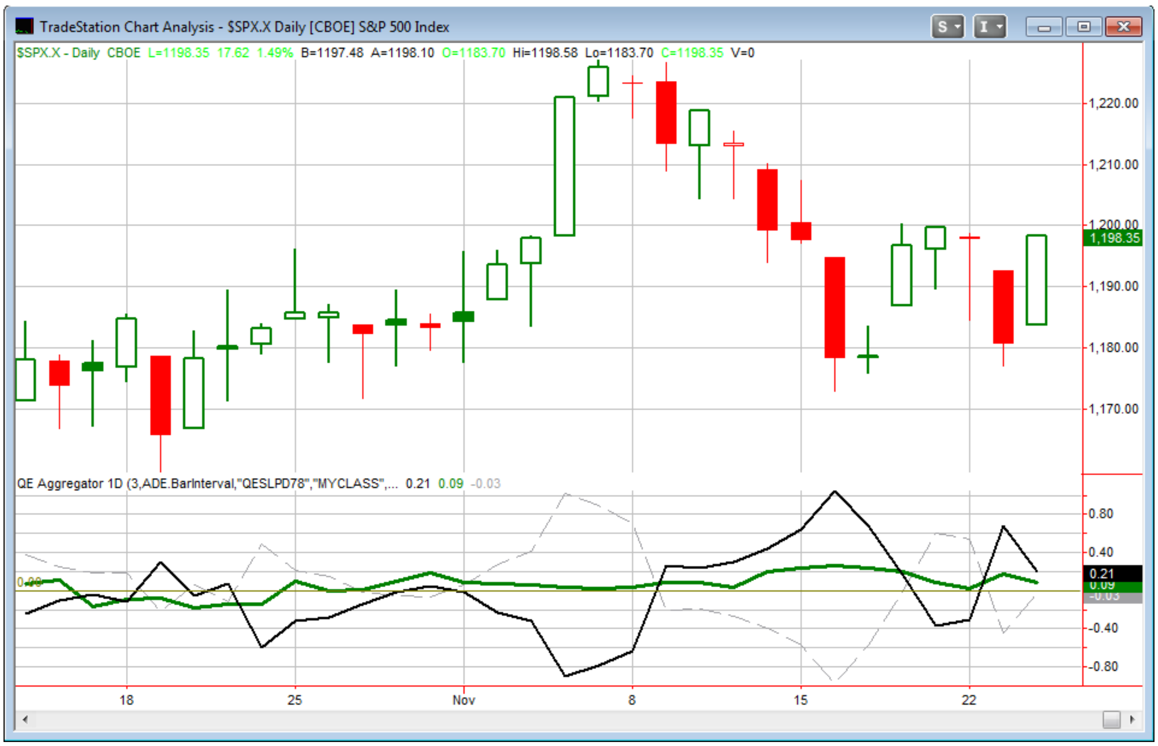
Not a huge edge but it still appeared worth considering. Below is the equity curve with a 3-day holding period.



I've seen smoother curves but this appears good enough for inclusion to me.

So we have a seasonally positive day on Friday, a seasonally negative day on Monday, volume indicative of a pullback and breadth indicative of a continuation higher. When indications get mixed like this I'm glad I have the Aggregator to weigh it all out.

I have updated the Aggregator chart below.



With some bearish evidence emerging the green Aggregator line dipped a little. It did still remain above 0 though. 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 also remained above 0. The positive value means the SPX has underperformed expectations over the last few days. So we have positive expectations and a market that is currently oversold. Historically this combination has provided a short-term bullish edge. A bullish configuration can be seen on the Aggregator chart whenever both lines are above 0. Due to this the Aggregator System remained long at the close.

The green Aggregator line is set up to remain positive tomorrow. This could change if strong bearish evidence emerges. Meanwhile, the Differential Pivot will be at 1,201.31. This means the SPX would only need to gain about 0.25% in order to switch from overbought to oversold and shift the Differential line below 0.

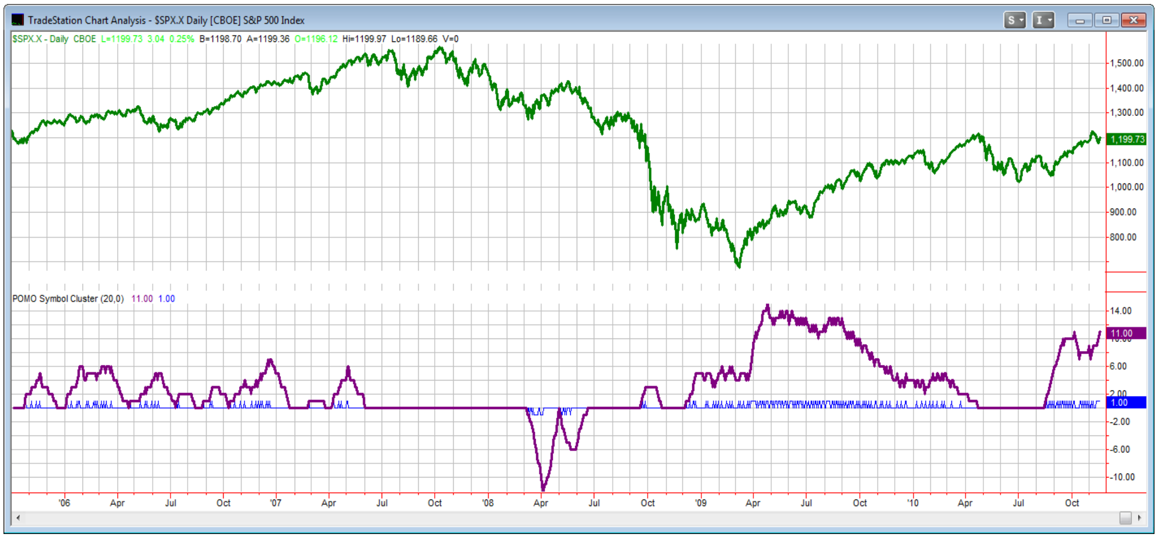
Though I considered it I did not lighten up at all on Wednesday afternoon. Should we see some more upside on Friday I will look to take some of my long exposure off the table. I am not looking to add any more today.

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/22 – bullish

I've seen a lot written lately about POMO days. POMO stands for Permanent Open Market Operations and it's the Fed's current method for trying to inject life (by injecting money) into the economy. They used to lower interest rates when they wanted to stimulate the economy but with interest rates already at zero that is no longer an option. It has been noted by a number of analysts that these liquidity injections appear to be stimulative for the stock market as well. Tom McClellan of McClellan Financial Publications wrote an excellent piece on POMO days a few weeks ago. Tom suggested that the liquidity injection may not take effect immediately and he looked at the how the market acted if there was a POMO within the last week rather than just being in the market on the day of the actual POMO. You can read his piece using the link below:

http://www.mcoscillator.com/learning_center/weekly_chart/pomo_the_hot_new_timing_tool

I decided to take my own look at POMO days. In doing so I decided to see how the market performed when a series of POMO days were clustered together. The assumption here is that if the Fed is regularly pumping money into the system it is more likely to have a bullish effect on the stock market than if there is just an occasional solitary injection. I examined different lookback periods. Below is a 20-day (approx 1-month) lookback period. It shows how many POMO days there have been in the last 20 days at any given point in time since August 0f 2005. This is as far back as data is available. (Data can be found on the Fed's website here.) The top line on the chart is the S&P 500.



It's a little tough to read on the chart, but there have now been 11 POMO days in the last 20 day period. This is as large a cluster as we have seen at any time other than the mid-April through mid-September pumping in 2009. That pumping coincided with a very strong stock market rally.

You'll note that in 2008 the POMO days cluster went negative. This is because the Fed went on a bit of a selling spree at that time. Those were days where they were selling securities rather than buying them. Since they were selling I represented them on my indicator as a negative day. As you can see the market did not perform too well after that period of Fed selling.

The tentative POMO day schedule is currently showing 11 more POMO buying days between now and December 9th, so we aren't likely to see a dip in the current cluster any time soon. To see possible implications I ran several studies examining performance after clusters had reached certain sizes. Below is a sample optimization report on some tests I ran.

Hold SPX if there are "POMO Days" number of POMO Days over the last "Days Back", offset "Offset" number of days. Go flat if the cluster of POMO Days is not large enough.

Days Back	Offset	POMO 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
18	0	5	56,271.24	299	170	129	56.86	982.02	-857.92	1.14	1.51	188.20
19	0	5	53,538.94	322	183	139	56.83	968.18	-889.49	1.09	1.43	166.27
20	0	5	39,932.49	348	192	156	55.17	951.73	-915.38	1.04	1.28	114.75
18	1	5	61,362.54	298	174	124	58.39	969.74	-865.91	1.12	1.57	205.91
19	1	5	46,969.64	321	180	141	56.07	964.00	-897.52	1.07	1.37	146.32
20	1	5	44,105.37	347	194	153	55.91	955.02	-922.67	1.04	1.31	127.10
18	0	6	40,800.84	224	130	94	58.04	934.71	-858.64	1.09	1.51	182.15
19	0	6	45,271.28	237	137	100	57.81	946.35	-843.79	1.12	1.54	191.02
20	0	6	42,200.09	252	143	109	56.75	919.70	-819.42	1.12	1.47	167.46
18	1	6	37,979.78	223	126	97	56.50	941.70	-831.69	1.13	1.47	170.31
19	1	6	39,857.89	236	134	102	56.78	917.66	-814.79	1.13	1.48	168.89
20	1	6	32,748.43	251	141	110	56.18	918.96	-880.22	1.04	1.34	130.47
18	0	7	40,380.97	199	114	85	57.29	990.66	-853.58	1.16	1.56	202.92
19	0	7	38,323.24	204	116	88	56.86	977.40	-852.90	1.15	1.51	187.86
20	0	7	40,972.87	209	120	89	57.42	969.64	-847.01	1.14	1.54	196.04
18	1	7	37,873.50	198	112	86	56.57	980.18	-836.13	1.17	1.53	191.28
19	1	7	39,732.76	203	116	87	57.14	965.25	-830.30	1.16	1.55	195.73
20	1	7	37,463.63	208	118	90	56.73	970.99	-856.82	1.13	1.49	180.11
18	0	8	38,068.85	170	95	75	55.88	1,064.24	-840.45	1.27	1.60	223.93
19	0	8	38,204.86	181	102	79	56.35	1,024.88	-839.65	1.22	1.58	211.08
20	0	8	39,237.94	191	109	82	57.07	990.37	-837.96	1.18	1.57	205.43
18	1	8	33,724.19	169	94	75	55.62	1,043.02	-857.60	1.22	1.52	199.55
19	1	8	35,504.11	180	101	79	56.11	1,013.12	-845.83	1.20	1.53	197.25
20	1	8	35,264.73	190	106	84	55.79	997.78	-839.28	1.19	1.50	185.60

The offset may be a little confusing so I'll explain that a little more. The assumption there is that even if the Fed buys treasuries today and pumps money into the banking system, that money will take at least a day to make its way into the stock market. So the offset of "1" is really looking at how big the cluster would have been as of yesterday. Results here are strong across the board. The best performing parameters would be to look for a cluster of at least 5 POMO (buying) days in an 18-day period, offset 1 day. This is a bit of an exercise in data mining and so picking the best results and assuming they will work as well in the future is dangerous.

Still, with positive results across the board during a period when the market was essentially flat it appears POMO activity by the Fed may have a bullish influence on the stock market. There is an old adage that says "Don't fight the Fed." It was written back in the days when interest rates would move up and down. But even with interest rates at 0, fighting the Fed appears to be a bad idea.

In the next week or so I'll hold a webinar discussion on POMO days to discuss these studies in a little more detail. Also, if there is sufficient interest I may add a chart to the website like the one shown above. For those who would like to read more on POMO days, both the Zerohedge and ETF Prophet sites have published research and information on them as well.

Other than POMO there was little in the way of studies with intermediate-term influence this past week. The pullback was a bit more extreme in terms of consecutive down days than is usually seen in an uptrend. There were some signs of panic early in the week as well. Still there doesn't appear to be bearish consequences as of yet. The only possible issue as I noted last week is that the number of new highs was lower at the recent peak than at the April peak. As of now that is a small complaint compared to the large amount of bullish evidence.

The market is still in an uptrend. We are in a seasonally strong period for the market. The Nasdaq continues to lead. And the Fed wants to help. I'll continue to favor the long side and trade extra selectively from the short side.

<u>Catapult and Capitulative Breadth Statistics</u>

Catapult & CBI Presentation Link

Open Catapult Triggers

GOOG – @ $603.29
GOOG –@ $595.47
GOOG –@ $583.72
MSFT –@ $25.81
ABT –@ $47.66
ABT –@ $46.95

Catapult for ETF's Trades

None

***Broad Market Large Cap CBI* – 6 (GOOG-3, MSFT, ABT-2)**

<u>Additional New Trade Ideas</u>

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.

No new entries tonight for me. There are a few systems triggers on the spreadsheet for those traders looking for more trade ideas.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
GOOG(1/3)	11/15/2010	$603.00	$594.97	-1.33%		Catapult
SPY(1/4)	11/16/2010	$118.16	$120.20	1.73%		Aggregator
GOOG(1/3)	11/16/2010	$593.39	$594.97	0.27%		Catapult
GOOG(1/3)	11/17/2010	$583.72	$594.97	1.93%		Catapult
MSFT(1/3)	11/17/2010	$25.81	$25.37	-1.70%		Catapult
ABT(1/3)	11/17/2010	$47.66	$46.96	-1.47%		Catapult
SPY(1/4)	11/23/2010	$118.45	$120.20	1.48%		sell on SPX close>1201.30
ABT(1/3)	11/24/2010	$46.95	$46.96	0.02%		Catapult

GOOG is close to triggering a Catapult exit. It would only need to gain about 2 points on Friday. Should this happen I would likely exit 2 of the 3 lots at the close and hold on to the last one for the standard exit at the next day's open.