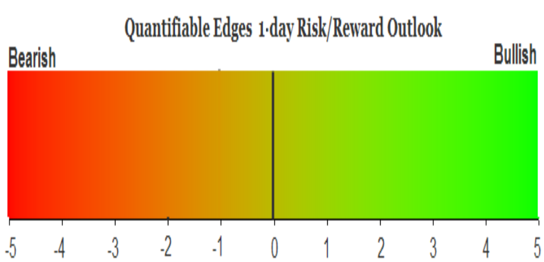
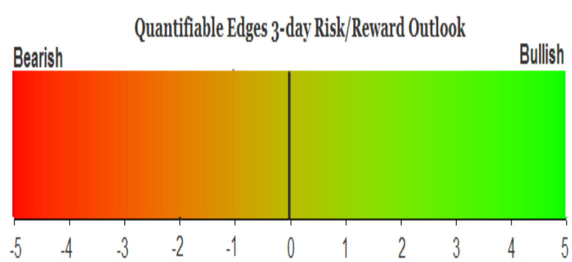
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

December 2, 2010 Volume 3 Issue 232

Market Overview





Tonight's Research Points

- Moves from a 5-day low to a 10-day high in 1 day often pull back short-term.
- Strong breadth and weak volume at a new high suggest a short-term bearish edge.
- 90% up days on declining volume has been followed by gains over the next 1-2 days but instances are low.
- 2 90% up days in one week have been followed by bullish intermediate-term returns in the past.
- The Aggregator System is flat.
- The NDX Aggressive Trend Timer is long.

Short-term Outlook
The Bottom Line

Wednesday's big rally moved the Aggregator System back to neutral as the market is now a bit overbought. Overall expectations remain positive though. I'm holding some long exposure but not looking to add anything tonight.

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				
December 2, 2010	10-day price & up vol% high. Low vol	1-3 days	Bearish	-1.10%
December 2, 2010	5-day low to 10-day high	1-2 days	Bearish	-1.30%
December 1, 2010	Pullback in uptrend at end of month	1-5 days	Bullish	2.30%
November 24, 2010	SPX down 1% Decliners 2x Advancers	1-9 days	Bullish	3.00%
Active - Long Term				
December 2, 2010	2 90% Up Volume % days in 5 days	1-16 days	Bullish	
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	
September 20, 2010	Nas/SPX RS favors Nasdaq	int term	Bullish	
Dropped Tonight				
November 29, 2010	Unfilled Gap Up then unfilled gap down	1-3 days	Bearish	-1.80%
November 24, 2010	***2 Unfilled Gaps Down in SPY***	***1-5 days***	***Bullish***	***2.10%***

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

The Evidence

The Aggregator was looking for a pop and it came in a big way on Wednesday. The market gapped up over 1% to start the day and never looked back. It opened strong and rallied for much of the morning. All the gains were reached by shortly after noon though. The last 4 hours of trading were marked by a sideways consolidation. And while the market couldn't muster any more gains, it didn't give much back either. QQQQ closed in the top half of its daily range and SPY closed in the top quartile. For the day the SPX, Nasdaq and Russell all gained between 2% and 2.25%. Breadth was very strong as the NYSE Up Issues % came in at 78% and the Up Volume % was 93%. Total volume started strong but tapered off with the afternoon consolidation and finished below Tuesday's levels.

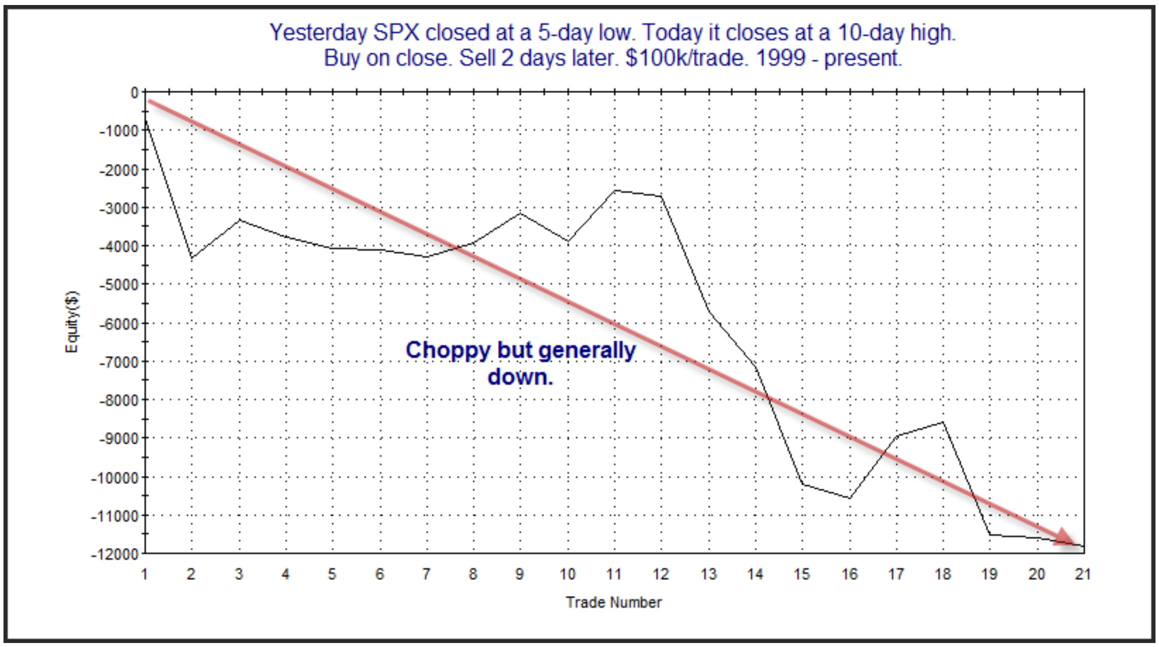
Some nights the studies send a clear message. Others it is more mixed and it takes a bit of judgment to wade through what's important and what isn't. Tonight the studies were mixed. Below is the evidence I found most compelling.

This first study was from the 5/27/09 blog. It looked at moves from a 5-day low to a 10-day high in 1 day. I've updated the results and run it from 1999 – present when the edge began to assert itself.

Yesterday SPX closed at a 5-day low. Today it closes at a 10-day high.
Buy 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	-17,959.01	21	10	11	47.62	1,109.69	-2,641.45	0.42	0.38	-855.19
4	-13,889.55	21	9	12	42.86	1,397.35	-2,205.48	0.63	0.48	-661.41
3	-10,137.87	21	12	9	57.14	949.88	-2,392.93	0.40	0.53	-482.76
2	-11,822.35	21	6	15	28.57	899.65	-1,148.02	0.78	0.31	-562.97
1	-4,124.97	21	11	10	52.38	555.86	-1,023.94	0.54	0.60	-196.43

Not a huge edge but one that I thought was at least worth a deeper look tonight. Below is the equity curve using a 2-day exit.



It isn't the smoothest equity curve I've ever seen but it does manage to chop its way lower. I think this study is worthy of consideration.

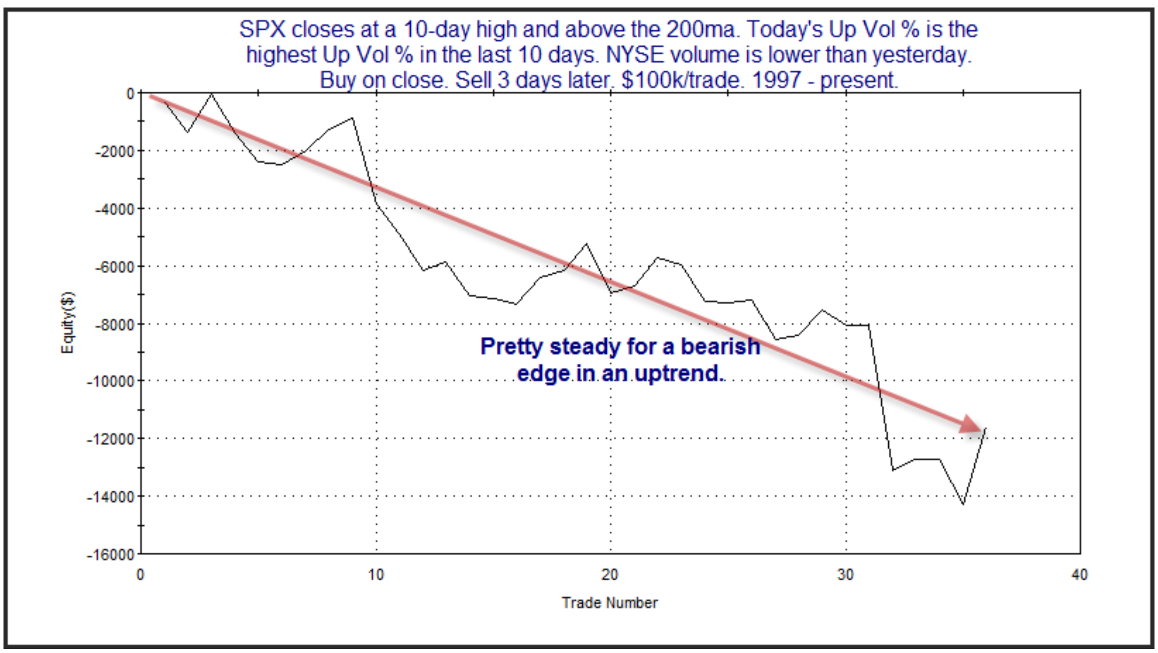
Another bearish study that arose looked at the new high on strong breadth and weak volume. I've updated the results from the 4/5/10 Subscriber Letter.

SPX closes at a 10-day high and above the 200ma. Today's Up Vol % is the highest Up Vol % in the last 10 days. NYSE volume is lower than yesterday. Buy on close. Sell X days later. $100k/trade. 1997 - 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	-8,586.77	33	16	17	48.48	1,660.19	-2,067.63	0.80	0.76	-260.21
9	-11,582.16	33	19	14	57.58	1,325.33	-2,625.96	0.50	0.68	-350.97
8	-15,549.17	33	17	16	51.52	1,154.98	-2,198.99	0.53	0.56	-471.19
7	-21,704.76	33	17	16	51.52	903.82	-2,316.86	0.39	0.41	-657.72
6	-17,325.73	34	17	17	50.00	713.26	-1,732.42	0.41	0.41	-509.58
5	-11,742.36	35	18	17	51.43	673.70	-1,404.06	0.48	0.51	-335.50
4	-10,239.39	35	16	19	45.71	748.37	-1,169.12	0.64	0.54	-292.55
3	-11,610.81	36	15	21	41.67	714.99	-1,063.60	0.67	0.48	-322.52
2	-6,970.29	36	18	18	50.00	491.56	-878.80	0.56	0.56	-193.62
1	-3,832.09	36	17	19	47.22	345.69	-510.99	0.68	0.61	-106.45

83% of instances posted a close below the entry price at some point in the next week.

Here too there appears to be a bit of a downside edge. It primarily comes from the outsized risk vs. reward since the % profitable is generally close to a coin toss. With this in mind I felt it important to check out the equity curve here as well.



Not perfect but not bad. I believe this study is also worthy of inclusion on the active list.

Not all studies suggested the strong breadth / weak volume combination was a bad thing though. Below is a study that looks at extreme breadth of at least 90% up volume while total volume declines. It was last published in the 9/21/10 Subscriber Letter.

NYSE Up Volume % > 90% while NYSE volume declines. SPX > 200ma.
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
11	6,960.86	10	6	4	60.00	3,498.36	-3,507.33	1.00	1.50	696.09
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

There is a hint of an upside edge here. Unfortunately the edge only appears on day 2 and the number of instances is too low to convince me this study is currently worth consideration. Below I've listed all instances using a 2-day exit strategy.

NYSE Up Volume % > 90% while NYSE volume declines. SPX > 200ma. Buy SPX on close. Sell 2 days later. $100k/trade. 1970 - present.				
Date/Time	**Signal**	**Price**	**% Profit**	**Run-up DrawDown**
11/23/84	Buy	$166.91	(0.38%)	$0.00
11/27/84	Sell	$166.28		($928.45)
11/20/86	Buy	$242.05	2.23%	$2,457.35
11/24/86	Sell	$247.44		($33.04)
01/02/87	Buy	$246.44	2.57%	$3,057.75
01/06/87	Sell	$252.77		$0.00
03/06/07	Buy	$1,395.41	0.46%	$888.92
03/08/07	Sell	$1,401.89		($338.67)
08/29/07	Buy	$1,463.76	0.70%	$1,204.28
08/31/07	Sell	$1,473.99		($850.68)
08/03/09	Buy	$1,002.63	0.01%	$444.51
08/05/09	Sell	$1,002.72		($823.68)
02/16/10	Buy	$1,094.87	1.09%	$1,216.67
02/18/10	Sell	$1,106.75		($13.65)
05/10/10	Buy	$1,159.73	1.03%	$1,130.04
05/12/10	Sell	$1,171.67		($1,033.72)
08/02/10	Buy	$1,125.86	0.12%	$254.32
08/04/10	Sell	$1,127.24		($800.80)
09/20/10	Buy	$1,142.71	(0.74%)	$506.34
09/22/10	Sell	$1,134.28		($968.31)

So the 90% breadth on lower volume just misses being convincing. But the fact that this was the 2nd 90% Up Volume day in a week appears positive. The scenario has historically been followed by more intermediate-term gains. The study below is from the 9/2/10 Subscriber Letter.

NYSE Up Volume > 90% for the 2nd time in a week. Buy SPX on close. Sell 15 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
20	55,935.41	11	9	2	81.82	6,663.22	-2,016.78	3.30	14.87	5,085.04
19	50,350.03	11	9	2	81.82	6,131.19	-2,415.33	2.54	11.42	4,577.28
18	51,202.50	11	9	2	81.82	6,104.50	-1,869.02	3.27	14.70	4,654.77
17	54,534.60	11	9	2	81.82	6,336.63	-1,247.55	5.08	22.86	4,957.69
16	60,195.74	12	11	1	91.67	5,527.30	-604.52	9.14	100.58	5,016.31
15	52,297.32	12	10	2	83.33	5,365.55	-679.08	7.90	39.51	4,358.11
14	50,688.66	12	11	1	91.67	4,694.85	-954.72	4.92	54.09	4,224.06
13	49,696.00	12	11	1	91.67	4,660.62	-1,570.80	2.97	32.64	4,141.33
12	31,970.92	13	10	3	76.92	4,200.29	-3,343.98	1.26	4.19	2,459.30
11	32,519.04	13	10	3	76.92	4,214.04	-3,207.13	1.31	4.38	2,501.46
10	34,155.17	13	10	3	76.92	4,334.98	-3,064.86	1.41	4.71	2,627.32
9	32,221.52	13	11	2	84.62	3,390.91	-2,539.27	1.34	7.34	2,478.58
8	26,824.31	13	11	2	84.62	3,137.40	-3,843.57	0.82	4.49	2,063.41
7	28,542.92	14	9	5	64.29	4,186.98	-1,827.98	2.29	4.12	2,038.78
6	8,576.35	14	7	7	50.00	3,318.31	-2,093.12	1.59	1.59	612.60
5	4,529.57	15	7	8	46.67	3,231.93	-2,261.74	1.43	1.25	301.97
4	14,382.37	15	7	8	46.67	3,252.07	-1,047.76	3.10	2.72	958.82
3	4,124.53	17	10	7	58.82	1,827.63	-2,021.69	0.90	1.29	242.62
2	-2,949.13	18	10	8	55.56	1,288.17	-1,978.85	0.65	0.81	-163.84
1	6,316.33	20	12	8	60.00	1,057.46	-796.65	1.33	1.99	315.82

The first 5 days show little to no edge as gains have been consolidated. Once you get out 13-16 days this study hits its sweet spot. Below I have updated the list of instances using 15-day exit criteria.

NYSE Up Volume > 90% for the 2nd time in a week. Buy SPX on close. Sell 15 days later. $100k/trade. 1970 - present.				
Date/Time	**Signal**	**Price**	**% Profit**	**Run-up DrawDown**
11/29/71	Buy	$93.41	8.71%	$8,709.80
12/20/71	Sell	$101.55		$0.00
08/20/82	Buy	$113.02	8.16%	$10,440.04
09/13/82	Sell	$122.24		($928.20)
08/02/84	Buy	$157.99	5.77%	$6,831.92
08/23/84	Sell	$167.11		$0.00
01/05/87	Buy	$252.19	6.91%	$11,388.96
01/26/87	Sell	$269.61		($23.76)
08/31/07	Buy	$1,473.99	2.97%	$4,338.25
09/24/07	Sell	$1,517.73		($2,324.90)
11/28/07	Buy	$1,469.01	(1.09%)	$3,710.08
12/19/07	Sell	$1,452.99		($2,268.48)
11/26/08	Buy	$887.68	(0.27%)	$3,491.04
12/18/08	Sell	$885.28		($8,062.88)
03/12/09	Buy	$750.74	11.14%	$12,617.71
04/02/09	Sell	$834.38		($1,101.24)
05/27/10	Buy	$1,103.06	1.31%	$1,615.50
06/18/10	Sell	$1,117.51		($5,480.10)
07/13/10	Buy	$1,095.34	2.29%	$2,908.36
08/03/10	Sell	$1,120.46		($3,499.86)
09/01/10	Buy	$1,080.29	4.12%	$6,278.08
09/23/10	Sell	$1,124.83		$0.00
09/24/10	Buy	$1,148.67	2.40%	$3,106.77
10/15/10	Sell	$1,176.19		($1,461.60)

One concern with this study is that 90% days have become much more common in the last few years. I've discussed this many times before and it is why I also track the Up Volume % Rank on the charts page. Today's Up Vol % was in the 96th percentile of all days over the last year. Last Wednesday's move was in the 94th percentile. Using these numbers I ran a test similar to the one above. Results showed no substantial edge. Of course 90% days were also common when each of the last 5 instances occurred and they all managed to follow through nicely. So I think this study is worth including on the intermediate-term Active Studies List but my enthusiasm for it is a bit tempered.

So two bearish studies made the short-term list tonight and we saw a bullish and a bearish leave the list. This has greatly reduced expectations.

I have updated the Aggregator chart below.

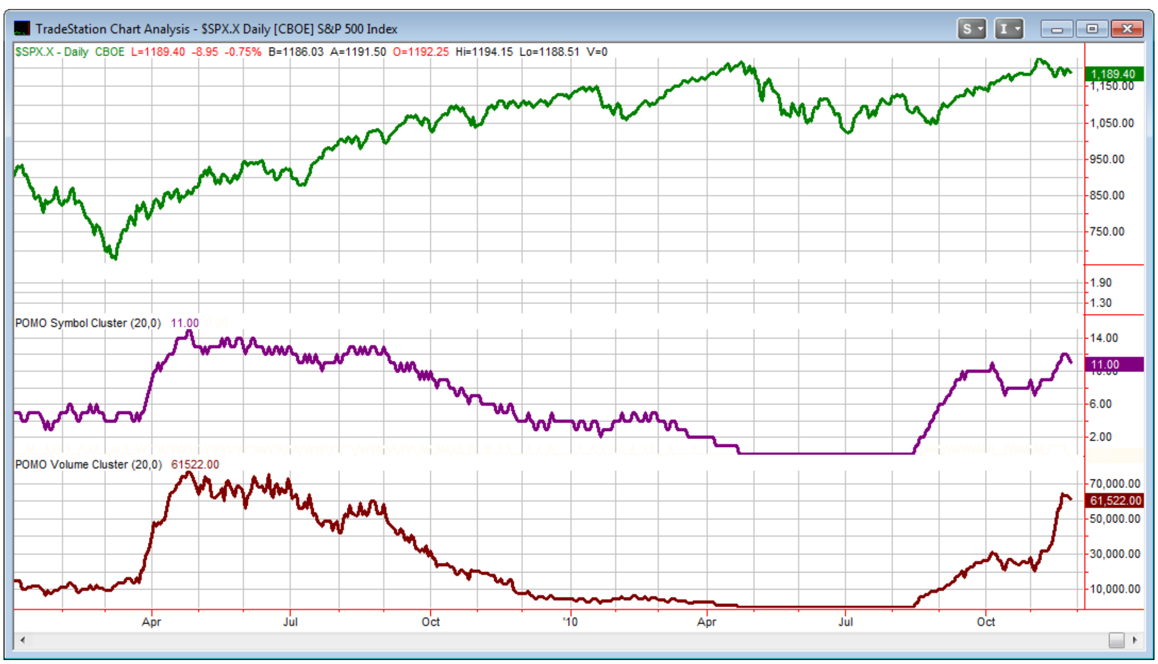
Despite the bearish tilt to the short-term studies tonight the green Aggregator line managed to hold above 0. A positive value indicates the net expectation from the Active Studies over the next few days is still for a mild move higher. Meanwhile today's rally caused the black Differential line to drop sharply and close below 0. The negative value means the SPX has outperformed expectations over the last few days. So we have positive expectations but a market that is already overbought. This is considered a neutral configuration. A neutral configuration can be seen on the chart whenever the Aggregator and Differential lines are on opposite sides of 0. Due to this the Aggregator System turned back to flat at the close.

The green Aggregator line is set up to remain positive tomorrow. This could change if more bearish evidence emerges. Meanwhile the Differential Pivot will be 1,189.33. This means the SPX would need to drop almost 1.4% in order for the Differential line to cross back above 0.

I took profits on a good amount of my positions at the close today. The GOOG catapult trade remains active and would need to put in a strong day tomorrow in order to trigger an exit. I am still holding 1 lot of SPY as well. With the intermediate-term outlook so bullish I've felt inclined to try and hold on to this lot for further gains. So far so good. Should the Aggregator System generate a short signal I will likely step out of this trade at least temporarily. For now I'll continue to ride it. I suspect the rally that began Wednesday could have quite a bit farther to go.

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/29 – bullish

Last week I discussed the possible effect of POMO Days in some detail. POMO stands for Permanent Open Market Operations and it is how the Fed goes into the open market to buy securities. The net effect of this buying is an influx of cash into the system. It appears a portion of that cash makes its way to the stock market and works as a bullish influence. A "POMO Day" is simply a day where these operations take place. Looking at the tentative schedule posted on the Fed's website it appears the next 9 trading days are ALL scheduled POMO days. It also appears the amount of buying will be quite large on most of these days. The chart below is updated from Tuesday night's letter. The top pane is the S&P 500. The middle pane is the rolling number of days in the last 20 that have been POMO days. The bottom pane is the total amount of money infused into the system over the previous 20 days.



As you can see both measures are already approaching levels as high as were reached during the summer of 2009, which contained the most amount of stimulus ever. Over the next 2 weeks the stimulus provided by both measures (days and $$) should exceed those 2009 levels. This should provide a substantially bullish influence over the next several weeks and possibly longer.

From a studies standpoint, there are now 6 intermediate-term studies on the active list. They cover POMO Days, breadth, price patterns, leadership (relative strength), and momentum. All of them are bullish. In fact the only potential issue I've noted over the past few weeks 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. European debt and Korean military action could provide additional shocks. These are difficult to quantify though and not something that factors into my decision making. I'll continue to favor the long side and trade extra selectively from the short side.

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

Open Catapult Triggers

GOOG – @ $603.29
GOOG –@ $595.47
GOOG –@ $583.72

Catapult for ETF's Trades

None

***Broad Market Large Cap CBI* – 3 (GOOG-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.

No new trade ideas tonight.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
GOOG(1/3)	11/15/2010	$603.00	$564.35	-6.41%		Catapult
SPY(1/4)	11/16/2010	$118.16	$121.01	2.41%		Aggregator
GOOG(1/3)	11/16/2010	$593.39	$564.35	-4.89%		Catapult
GOOG(1/3)	11/17/2010	$583.72	$564.35	-3.32%		Catapult
MSFT(1/3)	11/17/2010	$25.81	$26.04	0.89%		sold on close
ABT(1/3)	11/17/2010	$47.66	$47.01	-1.36%		sold on close
ABT(1/3)	11/24/2010	$46.95	$47.01	0.13%		sold on close
SPY(1/4)	11/30/2010	$118.49	$121.01	2.13%		sold on close
ABT(1/3)	11/30/2010	$46.09	$47.01	2.00%		sold on close

The MSFT, ABT and SPY trades were exited at the close as indicated in the intraday updates sent to gold subscribers Wednesday afternoon.