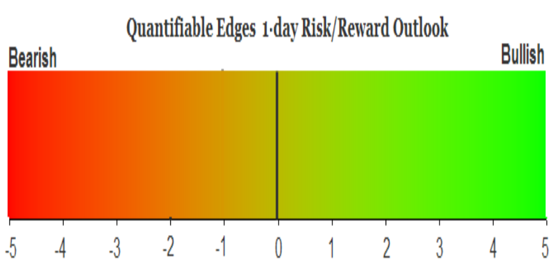
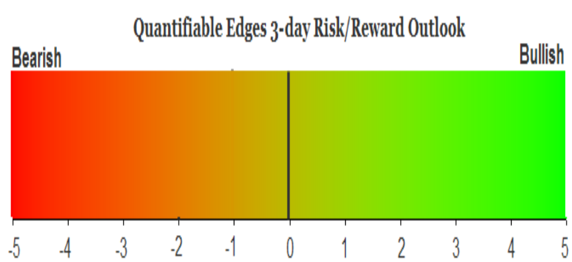
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

June 23, 2011 Volume 4 Issue 120

Market Overview





Signals Overview

Aggregator	Aggressive VIX	Conservative VIX	NDX Trend Timer
Flat	50% Long XIV	Flat	Flat

Tonight's Research Points

- Fed days that post new highs and then close poorly often bounce over the next few days.

Short-term Outlook
The Bottom Line

Evidence continues to favor the bulls but the market is currently overbought. Without a continued rally the overbought reading will wear off Thursday. I'm fairly neutral and awaiting a better edge.

Summary of Recent Active Studies (see Letters from listed dates for details)

Study Date	Description	Time span	Bias	Avg Max Move
Active				
June 23, 2011	Fed Day new high then reverse down	1-3 days	Bullish	2.05%
June 22, 2011	FTD with Up Issues % 1-yr Rank > 95%	1-3 days	Bullish	2.10%
Active - Long Term				
June 22, 2011	FTD with Up Issues % 1-yr Rank > 95%	int term	Bullish	
May 31, 2011	4 Weeks Down. Close > 40ma.	1-10 weeks	Bullish	9.00%
March 22, 2011	3 Days Up Issues % > 70%	8 months	Bullish	19.00%
November 22, 2010	POMO	int term	weakening	
October 25, 2010	SPX Golden Cross	int term	Bullish	
Dropped Tonight				
June 22, 2011	Fed Day	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

After gapping down to start the day the market fought its way back and actually had some gains in the early afternoon, but a late-day slide triggered by Bernanke comments made it a disappointing finish for the bulls. The SPX and Nasdaq both closed down 0.7% and the Russell 2000 lost 0.8%. Breadth was squarely negative as the NYSE Up Issues % came in at 42% and the Up Volume % was 29%. Total volume rose slightly from Tuesday's levels.

The action was not out of line for a Fed Day. The gap down filled easily as they almost always do. The market was trading higher at 2pm, which is when the bulk of the Fed Day bullish edge has already been realized, and Tuesday's high closing price suggested the edge wasn't as strong as it otherwise would have been. So the down close was not out of character either.

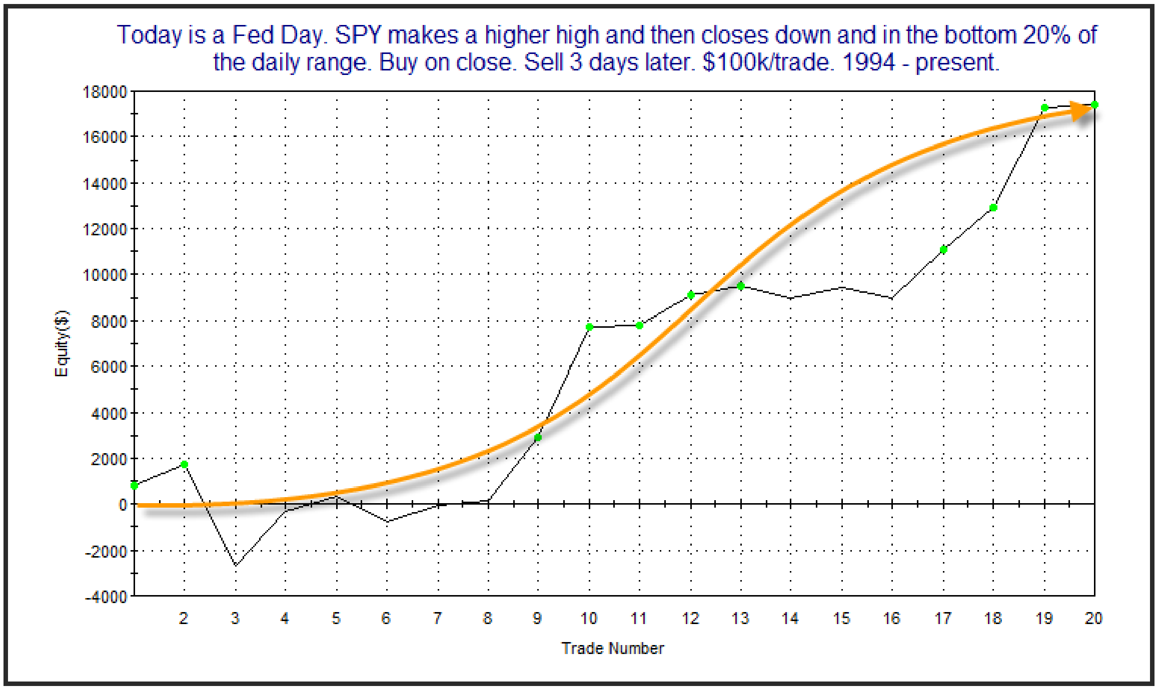
Therefore what we ended up with was a higher high that then reversed to close poorly. With emotions typically running higher, this type of action isn't too uncommon on a Fed Day. As is demonstrated by the study below, it has often been followed by a bounce.

Today is a Fed Day. SPY makes a higher high and then closes down and in the bottom 20% of the daily range. Buy on close. Sell X days later. $100k/trade. 1994 - 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	16,162.23	20	13	7	65.00	2,205.31	-1,786.69	1.23	2.29	808.11
4	22,019.97	20	12	8	60.00	2,582.36	-1,121.04	2.30	3.46	1,101.00
3	17,381.86	20	16	4	80.00	1,496.99	-1,642.48	0.91	3.65	869.09
2	13,873.58	20	15	5	75.00	1,548.59	-1,871.05	0.83	2.48	693.68
1	13,383.03	20	15	5	75.00	1,335.42	-1,329.66	1.00	3.01	669.15

19 of 20 instances (95%) closed above the Fed Day close at some point in the next 3 days.

The stats here suggest a bullish edge over the next 3-4 days. To get a better feel for how the edge has played out over time I produced an equity curve using a 3-day exit strategy.



For a setup with such a high winning percentage the equity curve sure appears choppy. It does go from lower left to upper right, so it isn't a complete disaster, but it does dampen my enthusiasm a little bit for this setup.

Of course Wednesday's high was not just higher than Tuesday, but was also a multi-day high. I ran some tests to see what impact this may have on results. In general I found they remained quite strong, though much, if not all, of the edge was exhausted by the end of day 1. The study below filters using a 5-day high. To get a few more instances I loosened the closing requirement from the bottom 20% to the bottom 25%.

Today is a Fed Day. SPY makes a 5-day high before reversing and closing negative and in the bottom 25% of its daily range.
Buy on close. Sell next day's close. $100k/trade. 1994 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
05/21/96	Buy	$67.55	0.95%	$962.00
05/22/96	Sell	$68.19		($236.80)
02/05/97	Buy	$77.64	0.67%	$720.72
02/06/97	Sell	$78.16		($296.01)
03/25/97	Buy	$78.75	0.43%	$1,154.79
03/26/97	Sell	$79.09		($469.53)
08/22/00	Buy	$150.25	0.50%	$684.95
08/23/00	Sell	$151.00		($704.90)
01/31/01	Buy	$137.02	0.66%	$677.97
02/01/01	Sell	$137.93		($561.33)
12/11/07	Buy	$147.91	0.99%	$2,609.36
12/12/07	Sell	$149.37		($479.96)
01/30/08	Buy	$134.91	1.77%	$2,689.83
01/31/08	Sell	$137.30		($1,267.11)
04/30/08	Buy	$138.26	2.07%	$2,067.78
05/01/08	Sell	$141.12		$0.00
10/29/08	Buy	$93.08	3.46%	$3,716.04
10/30/08	Sell	$96.30		($193.32)

We've seen longer winning streaks end over the last few years, but 9-0 is impressive and suggests an upside edge.

I have updated the Aggregator chart below.

The green Aggregator Line is still solidly above 0. Readings above 0 mean net expectations from the active list are for upside over the next few days. Meanwhile, the black Differential Line remains below 0. This means the SPX has outperformed expectations over the last few days. So net expectations are positive but the SPX is already a little overbought versus recent expectations. This is considered a neutral configuration. Neutral configurations can be seen on the chart whenever both lines close on opposite sides of 0. Due to this the Aggregator System remained flat at the close.

The green Aggregator line is again set to close above 0 on Thursday. This could change if bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,287.47. This is nearly even with Wednesday's close. So even a pause tomorrow would leave the SPX underperforming short-term expectations and cause the Differential Line to flip positive. Unless bearish evidence emerges, a flat or down close would likely trigger an Aggregator long signal.

Aside from the XIV position, I'm sidelined. I'm not going to rush into anything just yet either. Despite the Follow-Through Day on Tuesday the overall health of the market and the potential rally remains in doubt. The strong breadth on the FTD was a positive. Another sign to look for in the coming days is whether the upside momentum is able to persist. About 2/3 of the time the action in the first week after a FTD will predict whether that FTD leads to a successful rally or a failure. I'm going to give it one more day and see how things play out tomorrow before placing more capital at risk. Should the Aggregator System trigger a long trade I will likely look to begin scaling in on Friday.

Intermediate-term Outlook (2 weeks – 2 months)– updated 6/20 – neutral

The SPX closed higher this past week. In fact it closed higher on 4 of the 5 days. This sounds impossible since every day but Tuesday seemed disappointing, but it is true. From the 5/2 peak down to the low on Thursday the SPX declined 8.2%.

I conducted extensive research into IBD Follow-Through-Days (FTD) over the last few years. Much of it was published on the blog in 2008. Most of the work I published required an SPX correction of at least 8% before a FTD was looked for. Investors Business Daily followers and other intermediate-term trade will be eagerly awaiting a FTD before looking to aggressively allocate intermediate-term trend following positions to their portfolios.

That research is too vast to explore in detail in the letter, but I would suggest readers that are interested may want check out the links below.

This first one is a summary post with links to different areas of the research.

http://quantifiableedges.blogspot.com/2008/07/follow-through-days-quantified.html

This second link will bring up all blog posts with an "IBD Follow Through Day" label. There have been a few since the summary post above was published.

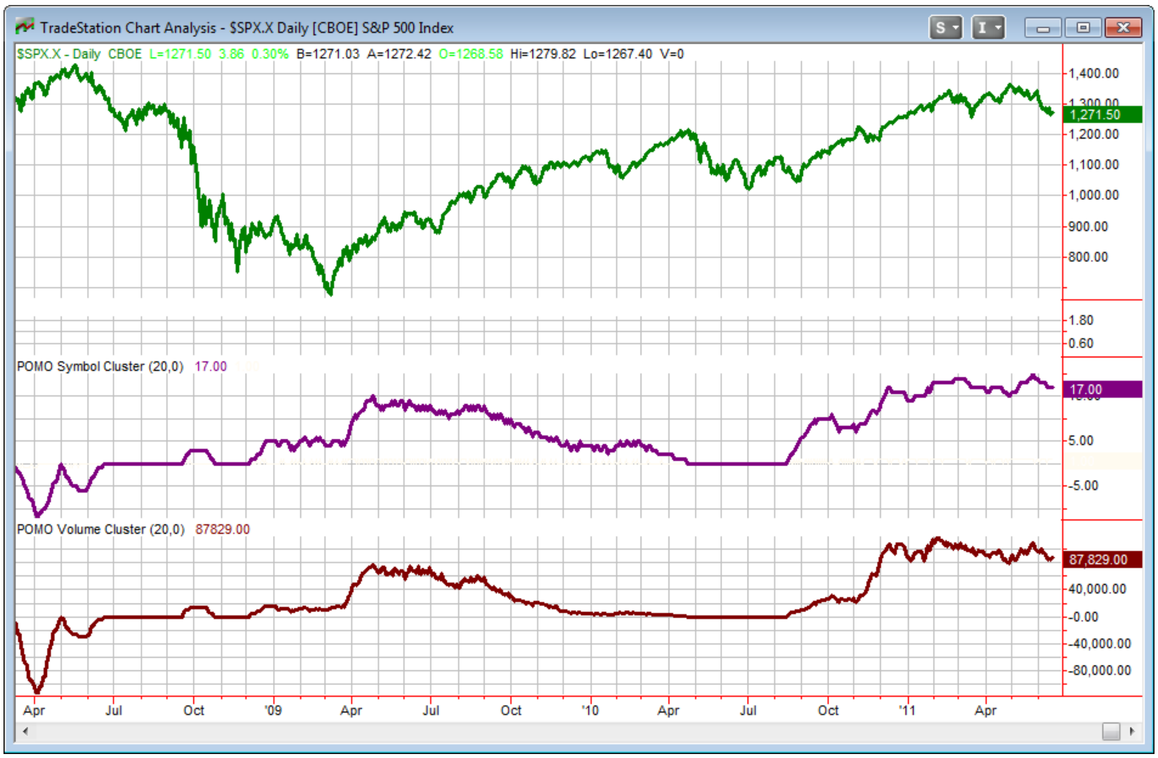
http://quantifiableedges.blogspot.com/search/label/IBD%20Follow%20Through%20Day

As bounces occur and FTDs are registered I will be sure to alert readers to odds and edges associated with FTDs.

I've been updating the POMO chart most weekends in the letter. For those who may not recall below is a brief refresher on POMO. Beneath that I have updated our POMO indicator chart.

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… The chart below (shows a couple of POMO indicators). 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. Information on acquiring the data and constructing the chart can be found in the January 3rd POMO presentation linked below. (Not available for trial users.)*

http://www.quantifiableedges.com/members/pomo.php



My POMO interpretation remains the same as last week.

Both the POMO Days and POMO Volume indicators remain at high levels. Still, they are beginning to trend lower. The current schedule calls for steady buying until the end of the month, but after that there will be little in the way of Fed stimulus. Starting July 1 we will see these indicators begin to head back towards the 0 line. There are 2 small days of buying currently scheduled in July which is associated with the reinvestment of principal payments rather than the $600billion of QE2 money. The past few times POMO stimulus was halted, it took the market about a month after the halt until prices began to decline.

For those that would like to view the current schedule I have provided a link below.

http://www.newyorkfed.org/markets/tot_operation_schedule.html

Intermediate-term studies are moderately bullish but we are certainly in the midst of a correction. Whether it turns into something worse or whether it straightens itself out quickly isn't yet clear. I expect we will get a bounce here in the short-term as suggested by the short-term section above. That bounce could carry forward for another few weeks. I don't have great confidence that it will surpass the May highs. My outlook remains neutral for now. This means I will approach both longs and shorts with some caution but am willing to bet either way should short-term evidence suggest an edge.

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

Open Catapult Triggers

None

Catapult for ETF's Trades

None

***Broad Market Large Cap CBI* – 0**

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.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
XIV	6/13/2011	$170.38	$165.58	-2.82%		