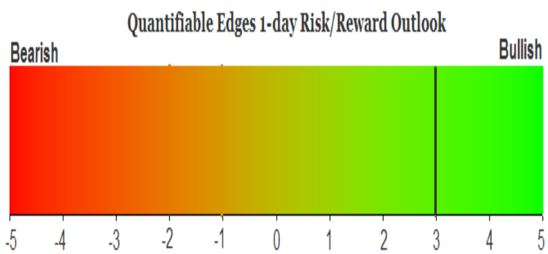
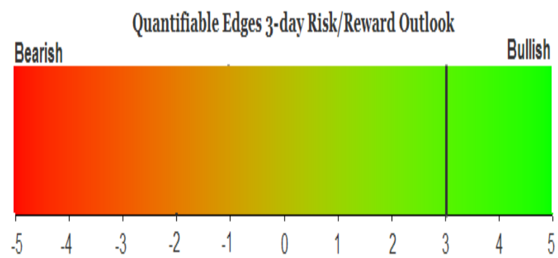
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 18, 2011 Volume 4 Issue 224

Market Overview





Signals Overview

Aggregator	Aggressive VIX	Conservative VIX	NDX Trend Timer
Long	100% Long XIV	100% Long XIV	Flat

Tonight's Research Points

- 2 days with an Up Issue % < 33.3% has consistently been followed by a bounce. Recent instances have been especially good.
- 2 days Up Issue % under 20% has been even more powerful.
- Thursday's triangle breakdown is a *potential positive* for the bulls.

Short-term Outlook

The Bottom Line

The market is now strongly oversold and evidence is squarely bullish. I am long and looking to get longer.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
November 18, 2011	Up Issues % < 33.3% 2 days < 200ma	1-2 days	Bullish	3.00%
November 17, 2011	1% Gap Down Fills & then collapses	1-3 days	Bullish	
November 17, 2011	SPX 1% drop. Decliners 2x advancers	1-3 days	Bullish	
Active - Long Term				
October 30, 2011	SPX & bond yields hit 50-day highs	1-50 days	Bearish	
October 19, 2011	50-day high on 90% up vol	1-50 days	Bullish	
October 19, 2011	FTD on strong breadth/20day high	int term	Bullish	
March 22, 2011	3 Days Up Issues % > 70%	8 months	Bullish	19.00%
Dropped Tonight				
November 16, 2011	***SPX up. VIX up. Midweek. SPX<20***	***1-4 days***	***Bearish***	
November 15, 2011	***Low vol. Narrow. Close>10 & < 200***	***1-3 days***	***Bearish***	

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

The Evidence

The selling from Wednesday continued on Thursday. The SPX fell 1.7%, the Nasdaq was down 2.0%, and the Russell 2000 declined 1.6%. Breadth was extremely negative as the NYSE Up Issues % came in at 19% and the Up Volume % was just 8%. Total NYSE volume rose for the 3rd day in a row.

In last night's letter I noted that although evidence was turning bullish we could still have another day or 2 of selling before the bounce. I explained that even though the 3-day estimates were bullish the 1-day estimates were negative and the 1-day risk/reward at the top of the letter was "0". Thursday's selling appears to have put the market in a place where a bounce *should* occur very shortly.

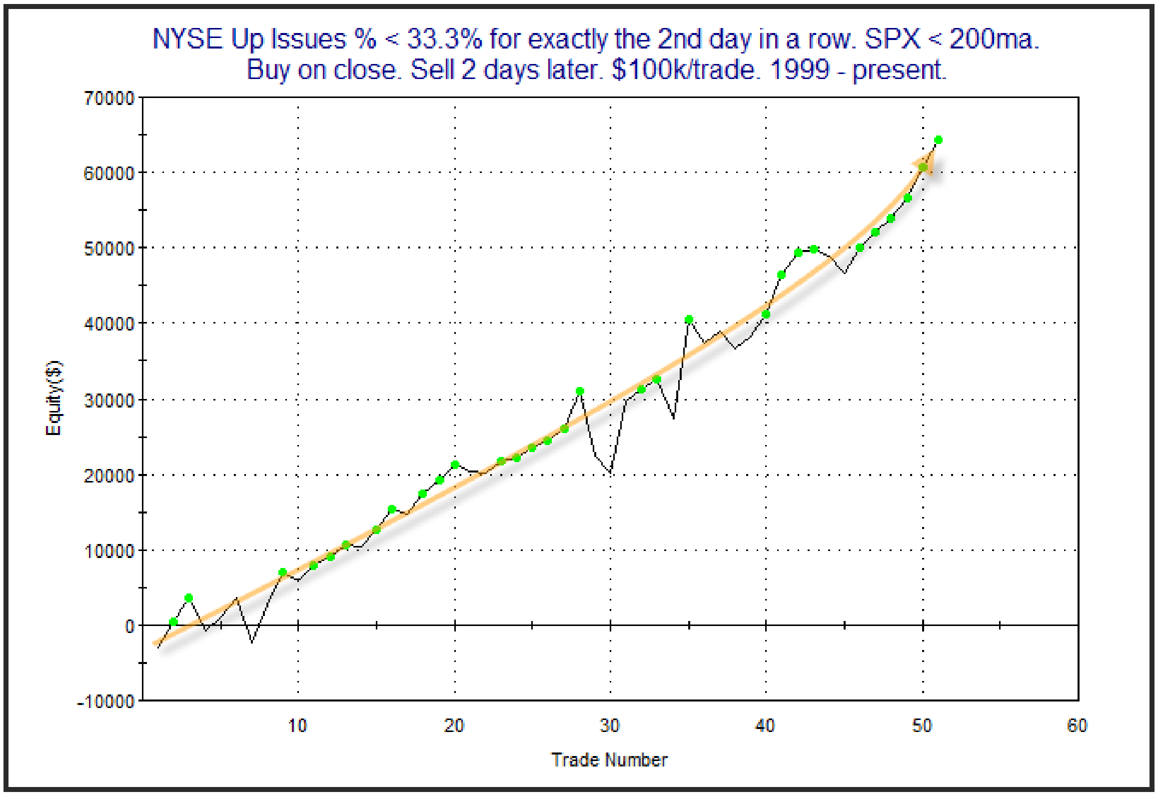
The study below was last seen in the 11/2/11 subscriber letter. It is one that I have shown many times over the last few years, and it has been incredibly dependable. The study looks for two days of strongly lopsided negative breadth and a close under the 200ma. I have updated the statistics.

NYSE Up Issues % < 33.3% for exactly the 2nd day in a row. SPX < 200ma.
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	70,550.01	45	33	12	73.33	3,221.55	-2,980.10	1.08	2.97	1,567.78
4	46,140.41	48	30	18	62.50	3,143.24	-2,675.38	1.17	1.96	961.26
3	52,290.55	51	32	19	62.75	3,573.20	-3,265.88	1.09	1.84	1,025.30
2	64,283.11	51	36	15	70.59	2,924.22	-2,732.59	1.07	2.57	1,260.45
1	43,193.26	51	34	17	66.67	2,004.42	-1,468.05	1.37	2.73	846.93

49 of 51 instances (96%) closed above the entry price
at some point in the next week.

For the considerable sample size and low number of criteria these results are astonishingly consistent. The stat at the bottom of the table is what seems most striking. Below is an equity curve using a 2-day exit.



As I've mentioned in the past I especially like this study because it has produced such consistently positive returns in a downtrending environment. That's fairly unusual to see.

You'll note that the last several instances have really done well. And if you have been reading Quantifiable Edges over the past few months you'll likely recognize this study. We've seen it a lot. Below is a chart showing the setup and a 2-day exit over the past few months.

It won't always work this well, but I'd sure like to see it happen again here.

Of course breadth the last two days was well below the 33% threshold. Therefore, as I also did in the 11/2/04 letter I decided to examine the results under these even more extreme conditions. This test is the same as the one above except I lowered the threshold from 33% to 20%. (Results are updated.)

NYSE Up Issues % < 20% for exactly the 2nd day in a row. SPX < 200ma.
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	59,080.41	9	9	0	100.00	6,564.49	0.00	100.00	100.00	6,564.49
4	44,488.62	9	8	1	88.89	6,284.05	-5,783.80	1.09	8.69	4,943.18
3	30,092.59	9	7	2	77.78	5,777.98	-5,176.65	1.12	3.91	3,343.62
2	26,166.22	9	8	1	88.89	4,349.65	-8,631.00	0.50	4.03	2,907.36
1	22,723.77	9	8	1	88.89	2,981.60	-1,129.00	2.64	21.13	2,524.86

While instances are a little low the numbers are astounding. A week out all nine instances were trading higher and the average gain was close to 6.5%. As you might suspect with gains this large there was a fair amount of variance. Below I have listed all 9 instances.

NYSE Up Issues % < 20% for exactly the 2nd day in a row. SPX < 200ma. Buy on close. Sell 5 days later. $100k/trade. 1999 - present.				
Date/Time	**Signal**	**Price**	**% Profit**	**Run-up Drawdown**
07/23/02	Buy	$797.70	13.17%	$14,013.75
07/30/02	Sell	$902.78		($2,752.50)
08/15/07	Buy	$1,406.70	4.08%	$4,129.36
08/22/07	Sell	$1,464.07		($2,563.10)
03/17/08	Buy	$1,276.60	5.98%	$6,480.24
03/25/08	Sell	$1,352.98		$0.00
10/07/08	Buy	$996.23	0.18%	$4,808.00
10/14/08	Sell	$998.01		($15,643.00)
11/06/08	Buy	$904.88	0.71%	$5,177.70
11/13/08	Sell	$911.29		($9,480.90)
11/20/08	Buy	$752.44	19.11%	$18,982.92
11/28/08	Sell	$896.24		($1,453.32)
09/22/11	Buy	$1,129.56	2.73%	$5,834.40
09/29/11	Sell	$1,160.40		($721.60)
10/03/11	Buy	$1,099.23	8.70%	$8,611.20
10/10/11	Sell	$1,194.89		($2,201.40)
11/01/11	Buy	$1,218.28	4.73%	$4,860.14
11/08/11	Sell	$1,275.92		$0.00

I would be a little surprised to see the market gain close to 6.5% in the next week, but the potential for a sizable bounce is certainly there.

It is also notable that the triangle breakdown occurred today. I've discussed the propensity of triangle breaks to reverse the last couple of days. Now we finally have the break. As the triangle study available on the downloads page was designed the downside target for a "successful" triangle breakdown would be 1,153.29. But about 70% of the triangle breaks failed. This suggests we have a much better chance of seeing 1,266.99 (which would mark a "failure") before we see 1,153.29. That's supportive for the bullish case.

I have updated the Aggregator chart below.

With tonight's studies the green Aggregator Line moved higher into positive territory. Readings above 0 mean net expectations from the Active List are for upside over the next few days. Meanwhile, the strong selling caused the black Differential Line to also remain strongly above 0. A positive Differential reading means the SPX has underperformed expectations over the last few days. So net expectations are bullish and the SPX is oversold versus recent expectations. Historically this combination has provided an upside edge. It can be seen on the chart whenever both lines close above 0. Tonight's movement caused the Aggregator System to remain long at the close. This was posted to the systems page before the bell.

Based on the current studies the Aggregator Line would remain positive on Friday. It will take some very compelling bearish evidence to change this. Meanwhile the Differential Pivot will be 1,249.57 on Friday. This is 2.75% above Thursday's close. So the SPX will need to close up at least this much in order for the Differential Line to drop back below 0. It's unlikely we will see that happen in 1 day. Most likely the market will need to register a multi-day bounce or consolidation in order for the oversold condition to wear off.

As I suspected I was a bit early on the 1st portion of this trade. But with tonight's studies and next week's positive Thanksgiving seasonality I am looking to position more aggressively. I'll discuss Thanksgiving seasonalities over the weekend. If you want a sneak preview, check out the 11/22/10 subscriber letter on the archives page or use the link below.

2010-11-22 QE Subscriber Letter.pdf

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/14 – bullish

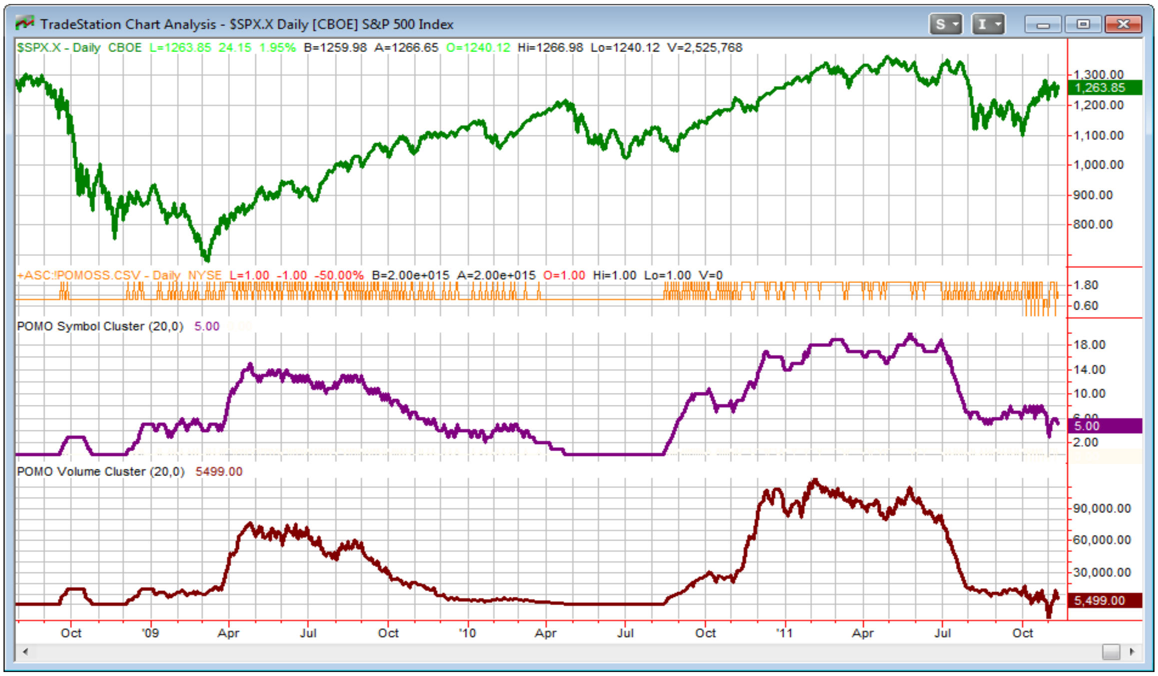
Action this week saw the market rise some overall, but the range was completely inside the previous week's range. At this point the market is nearing the October highs and could make an attempt at another leg up.

The inside week action failed to give anything new and compelling in the way of intermediate-term studies. The majority of those studies remain bullish and despite the fact that the market is still below its 200ma, the uptrend since early October appears to be in place (though weaker).

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 (purple) pane is the net rolling number of days in the last 20 that have been POMO days. In other words, a day the Fed buys on the market will add +1 while a day of selling will count as -1. The bottom pane is the total amount of money infused into (or taken out of) 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



This week we saw 3 days of buying and 1 day of selling activity from the Fed. The buy amounts were stronger than the selling amount as well. So there was net liquidity injected and the POMO Volume Cluster indicator rose nicely. We are still seeing very mild readings.

There was a strong thrust in the market that began at basically the same time as Operation Twist. It is now clear that Operation Twist will not provide a liquidity injection similar to QE1 or QE2. The POMO Volume indicator even dipped briefly into negative territory last week. We'll see if Operation Twist can continue to act as a positive influence or if the market falters without much liquidity being injected into the system.

Overall there still appears to be more favoring the bulls at this point than the bears. I'm currently considering POMO activity as neutral. Bears can look to our SPX/TNX study from a couple of weeks ago to support their case. Bullish evidence is based on price and breadth thrusts from last month as well as the positive aspects of the IBD Follow Through Day in October. I think this rally has further to go, and we will soon be entering a very bullish time of year for the market. So as I mentioned above, I'm more inclined to favor longs than shorts. I also may look to hold some longs a bit longer if circumstances allow.

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.

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SPY - buy ¼ index position @ $122.11 limit. Based on short-term outlook above. I will continue to scale in.

SPY - buy ¼ index position @ $121.50 limit ON CLOSE. If the market continues lower on Friday I want to get in a sizable amount. In addition to the oversold conditions, Thanksgiving week is seasonally strong (especially Wed and Fri). I'll discuss this more over the weekend, but I want to get a 3rd lot on if SPY closes poorly.

XIV - buy ½ size trading position @ $5.00 limit. I'll look to put the 2nd half of this trade on as well.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
HNZ	***11/7/2011***	***$52.65***	***$52.82***	***0.32%***		***90609 exit triggered***
SPY(1/4)	11/17/2011	$123.85	$122.11	-1.40%		bought on open
XIV(1/2)	11/17/2011	$5.21	$5.03	-3.45%		bought on open

The 90609 exit triggered at the close, making for a profitable but disappointing trade.