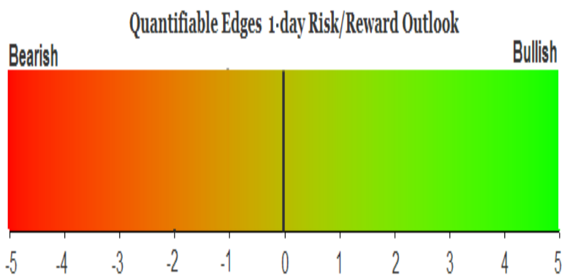
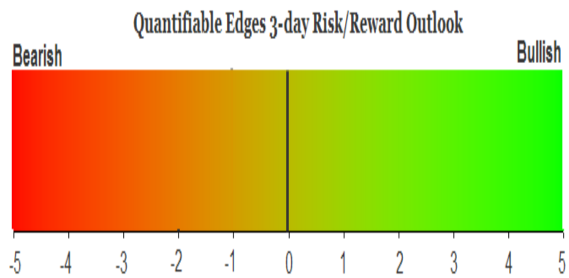
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 14, 2012 Volume 5 Issue 178

Market Overview





Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Flat	50% Long XIV	Short	Flat

Tonight's Research Points

- Strong breadth and volume at a new high are nice, but not terribly compelling when not emerging from a basing pattern.
- 100-day highs on Fed Days have often led to follow-on buying.
- QE3 is here and the rules are going to change some…

Short-term Outlook

The Bottom Line

The market looks strong but is strongly overbought. I'm waiting the next compelling opportunity.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
September 14, 2012	20-high on 20-high vol	1-3 days	Bullish	
September 14, 2012	100 day high on Fed Day	1-8 days	Bullish	1.90%
September 10, 2012	%b > 115 2 days	1-5 days	Bullish	1.80%
September 10, 2012	200-high on 1st Friday	1-6 days	Bearish	
Active - Long Term				
September 11, 2012	Key Reversal from high	1-12 days	Bullish	
September 10, 2012	POMO liquidity temporarily contracting	int term	Bearish	
September 5, 2012	Russell up 1%. SPX down	1-10 days	Bearish	
August 20, 2012	Nasdaq leading SPX	int term	Bullish	
July 30, 2012	SPX 50-day high on 90% up vol	1-50 days	Bullish	
February 1, 2012	Golden Cross	int term	Bullish	
Dropped Tonight				
September 12, 2012	Inside day with unfilled gap up	1-2 days	Bearish	
September 7, 2012	***50-high break strong breadth & vo***	***1-5 days***	***Bullish***	
September 7, 2012	***Breakout with unfilled gap up***	***1-5 days***	***Bullish***	
September 11, 2012	***20-high poor close***	***1-8 days***	***Bullish***	***2.00%***

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

The Evidence

Boom. The Fed announced QE3 and the market loved it. The SPX rose 1.6%, and the NASDAQ and the Russell 2000 each rallied 1.3%. Breadth was extremely positive as the NYSE Up Issues % was 77% and Up Volume % came in at 91%. Total NYSE volume came in at the highest level since early August.

Lots to cover. Let's first start with the price/breadth/volume stuff and then I'll discuss the Fed.

The study below is from just a week ago in the 9/7/12 letter. It examined breakouts to new highs on the highest volume in a month. Op-ex Fridays were excluded because they typically have very high volume. Results are updated. (But note that Thursday did not quite qualify.)

SPX closes at a 20-day high after not having done so for at least 10 days. Close > 200ma.
NYSE volume is the highest in 20 days. It is not op-ex Friday.
Buy SPX on close. Sell X days later. $100k/trade. 1993 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	26,221.61	11	9	2	81.82	3,217.90	6,645.00	-1,369.75	-1,518.22	2.35	10.57	2,383.78
19	28,727.21	11	9	2	81.82	3,454.97	6,957.50	-1,183.76	-2,336.29	2.92	13.13	2,611.56
18	33,817.48	11	9	2	81.82	3,956.76	6,622.50	-896.69	-1,503.48	4.41	19.86	3,074.32
17	34,943.80	11	10	1	90.91	3,673.34	6,003.20	-1,789.57	-1,789.57	2.05	20.53	3,176.71
16	36,364.59	11	9	2	81.82	4,211.60	5,887.44	-769.89	-1,470.65	5.47	24.62	3,305.87
15	34,747.48	11	9	2	81.82	4,181.26	6,105.00	-1,441.92	-2,393.24	2.90	13.05	3,158.86
14	31,910.80	11	9	2	81.82	3,776.70	6,007.40	-1,039.77	-1,680.36	3.63	16.35	2,900.98
13	29,499.88	11	10	1	90.91	3,013.77	5,741.66	-637.78	-637.78	4.73	47.25	2,681.81
12	25,791.83	11	10	1	90.91	2,585.75	5,978.75	-65.66	-65.66	39.38	393.81	2,344.71
11	27,294.53	11	11	0	100.00	2,481.32	5,250.00	0.00	0.00	100.00	100.00	2,481.32
10	23,913.43	11	10	1	90.91	2,476.97	4,885.00	-856.26	-856.26	2.89	28.93	2,173.95
9	25,045.10	11	11	0	100.00	2,276.83	5,451.25	0.00	0.00	100.00	100.00	2,276.83
8	21,240.96	11	9	2	81.82	2,415.03	3,842.50	-247.17	-450.24	9.77	43.97	1,931.00
7	19,695.44	11	9	2	81.82	2,336.78	4,443.12	-667.79	-811.65	3.50	15.75	1,790.49
6	16,646.32	11	9	2	81.82	2,095.84	4,698.80	-1,108.11	-2,094.42	1.89	8.51	1,513.30
5	19,088.18	12	10	2	83.33	2,061.60	4,683.84	-763.91	-1,360.77	2.70	13.49	1,590.68
4	14,956.20	12	10	2	83.33	1,613.33	4,518.75	-588.55	-1,043.86	2.74	13.71	1,246.35
3	10,457.41	12	10	2	83.33	1,222.18	2,403.80	-882.17	-1,369.04	1.39	6.93	871.45
2	5,308.33	12	7	5	58.33	1,056.14	1,998.39	-416.94	-1,301.14	2.53	3.55	442.36
1	8,881.39	12	10	2	83.33	980.38	1,606.89	-461.21	-645.21	2.13	10.63	740.12

Results are very strong. But while most filters are met, Thursday was not preceded with a 10-day basing period. So tonight I looked at instances like Thursday that were not fresh breakouts. Those results are below.

SPX closes at a 20-day high. It also made a 20-day high at least once in the previous 10 days. Close > 200ma. NYSE volume is the highest in 20 days. It is not op-ex Friday. Buy SPX on close. Sell X days later. $100k/trade. 1993 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	48,871.60	22	19	3	86.36	2,928.97	6,447.84	-2,259.62	-4,137.71	1.30	8.21	2,221.44
19	48,390.31	22	19	3	86.36	2,941.20	6,379.16	-2,497.48	-4,532.28	1.18	7.46	2,199.56
18	41,828.89	22	19	3	86.36	2,617.50	5,997.88	-2,634.54	-5,186.38	0.99	6.29	1,901.31
17	42,345.03	22	19	3	86.36	2,702.76	5,665.56	-3,002.49	-4,998.59	0.90	5.70	1,924.77
16	40,889.15	22	19	3	86.36	2,486.23	5,316.64	-2,116.38	-3,266.28	1.17	7.44	1,858.60
15	41,578.29	23	17	6	73.91	2,796.64	5,280.54	-994.09	-2,595.30	2.81	7.97	1,807.75
14	39,282.95	23	20	3	86.96	2,255.91	4,999.68	-1,945.09	-2,273.70	1.16	7.73	1,707.95
13	38,288.19	23	19	4	82.61	2,350.94	4,789.50	-1,594.90	-2,762.97	1.47	7.00	1,664.70
12	31,515.19	23	18	5	78.26	2,203.44	4,951.21	-1,629.34	-2,992.08	1.35	4.87	1,370.23
11	27,687.55	23	18	5	78.26	2,040.68	5,026.96	-1,808.96	-3,677.70	1.13	4.06	1,203.81
10	23,327.85	23	16	7	69.57	2,135.02	4,304.04	-1,547.50	-3,411.90	1.38	3.15	1,014.25
9	24,452.23	23	17	6	73.91	1,991.60	3,941.96	-1,567.50	-3,097.47	1.27	3.60	1,063.14
8	22,832.68	23	17	6	73.91	1,926.24	4,503.68	-1,652.24	-2,963.67	1.17	3.30	992.73
7	19,918.30	24	18	6	75.00	1,439.83	2,907.80	-999.78	-2,268.24	1.44	4.32	829.93
6	18,097.37	24	19	5	79.17	1,441.80	2,721.95	-1,859.36	-4,691.70	0.78	2.95	754.06
5	10,913.07	24	16	8	66.67	1,305.72	2,489.51	-1,247.31	-2,959.32	1.05	2.09	454.71
4	12,771.72	25	16	9	64.00	1,327.24	3,276.08	-940.45	-2,560.74	1.41	2.51	510.87
3	14,211.44	27	18	9	66.67	1,195.75	3,578.64	-812.46	-1,553.21	1.47	2.94	526.35
2	6,933.46	28	19	9	67.86	686.27	1,593.78	-678.40	-1,421.00	1.01	2.14	247.62
1	201.57	33	17	16	51.52	396.17	1,109.66	-408.34	-1,099.82	0.97	1.03	6.11

The edge does not appear as pronounced here but there still appears to be an upside tendency – for both the short and intermediate-term.

The breadth was also remarkable, and another study from the 9/7/12 letter examined 50-day highs on 90% up volume. It is also updated below.

SPX closes at a 50-day high. NYSE Up Volume > 90%.
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: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
50	87,196.79	17	16	1	94.12	5,791.93	19,845.80	-5,474.10	-5,474.10	1.06	16.93	5,129.22
45	85,183.93	18	16	2	88.89	5,830.07	17,945.20	-4,048.58	-5,052.36	1.44	11.52	4,732.44
40	83,320.36	19	15	4	78.95	5,989.19	20,950.80	-1,629.39	-2,937.98	3.68	13.78	4,385.28
35	86,607.69	19	16	3	84.21	5,695.52	18,961.80	-1,506.89	-2,194.86	3.78	20.16	4,558.30
30	74,210.36	19	17	2	89.47	4,411.97	11,920.74	-396.52	-418.88	11.13	94.58	3,905.81
25	64,737.87	21	16	5	76.19	4,670.71	12,045.67	-1,998.68	-3,024.54	2.34	7.48	3,082.76
20	58,803.67	22	16	6	72.73	4,654.12	13,393.77	-2,610.37	-6,770.72	1.78	4.75	2,672.89
15	50,114.95	22	17	5	77.27	3,923.24	8,150.48	-3,316.01	-6,277.02	1.18	4.02	2,277.95
10	33,393.72	24	15	9	62.50	3,263.16	10,507.25	-1,728.18	-4,090.24	1.89	3.15	1,391.40
9	28,463.36	24	16	7	66.67	2,846.31	8,413.73	-2,439.66	-5,207.55	1.17	2.67	1,185.97
8	28,439.04	24	16	8	66.67	2,942.48	8,524.75	-2,330.07	-4,082.16	1.26	2.53	1,184.96
7	26,187.46	25	16	9	64.00	2,848.23	6,026.80	-2,153.79	-3,954.60	1.32	2.35	1,047.50
6	26,565.22	25	17	8	68.00	2,231.22	6,819.80	-1,420.68	-4,106.70	1.57	3.34	1,062.61
5	32,549.01	28	22	6	78.57	1,828.56	8,516.82	-1,279.87	-3,295.50	1.43	5.24	1,162.46
4	23,065.27	29	22	7	75.86	1,651.36	6,716.71	-1,894.95	-4,894.50	0.87	2.74	795.35
3	15,741.61	29	19	10	65.52	1,463.02	6,740.50	-1,205.57	-5,105.87	1.21	2.31	542.81
2	17,265.74	29	20	9	68.97	1,138.89	4,028.44	-612.44	-2,409.33	1.86	4.13	595.37
1	10,825.14	31	17	14	54.84	960.96	2,755.52	-393.66	-1,255.50	2.44	2.96	349.20

While returns are very strong, this study does not have a basing period requirement. I added a filter similar to the last study to see how the short-term has played out if it was not a fresh breakout.

SPX closes at a 50-day high. NYSE Up Volume > 90%.
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: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	4,968.23	13	8	5	61.54	1,721.37	4,217.92	-1,760.55	-3,453.06	0.98	1.56	382.17
9	2,080.60	13	9	4	69.23	1,393.98	3,174.20	-2,616.30	-5,207.55	0.53	1.20	160.05
8	5,784.28	13	9	4	69.23	1,696.19	4,835.70	-2,370.36	-4,082.16	0.72	1.61	444.94
7	5,467.54	15	9	6	60.00	1,789.57	4,796.01	-1,773.10	-2,724.73	1.01	1.51	364.50
6	5,833.74	15	9	6	60.00	1,369.57	3,077.36	-1,082.07	-2,414.72	1.27	1.90	388.92
5	8,419.74	16	13	3	81.25	894.18	2,350.02	-1,068.20	-1,804.88	0.84	3.63	526.23
4	8,638.21	18	14	4	77.78	1,145.86	2,418.90	-1,850.94	-3,595.13	0.62	2.17	479.90
3	-4,971.45	18	9	9	50.00	645.40	1,154.34	-1,197.79	-5,105.87	0.54	0.54	-276.19
2	197.89	18	10	8	55.56	506.75	1,351.90	-608.70	-2,409.33	0.83	1.04	10.99
1	-1,038.05	18	7	11	38.89	524.89	1,646.28	-428.39	-1,255.50	1.23	0.78	-57.67

In this case there no longer appears to be a substantial short-term upside edge.

The move higher has a better chance to continue thanks to the strong volume and the strong breadth, but the upside edge is greatly reduced (and nearly eliminated) being that the market was already extended.

In "The Quantifiable Edges Guide to Fed Days" I discussed Fed Days that close at new highs. The basic finding was that when the market closed at a short-term high on a Fed Day, then it was likely to pull back over the next few days. But when it closed at a long-term high, then the rally was likely to continue. Below is a study from the guide that last appeared in the 3/14/12 Subscriber Letter.

SPX closes at a 100-day high on a Fed Day.
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: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	26,212.88	25	19	6	76.00	1,799.18	5,492.11	-1,328.57	-2,161.08	1.35	4.29	1,048.52
9	28,164.35	25	20	5	80.00	1,815.29	5,708.74	-1,628.30	-2,346.69	1.11	4.46	1,126.57
8	29,187.27	25	21	4	84.00	1,472.30	3,995.65	-432.78	-854.00	3.40	17.86	1,167.49
7	22,202.84	25	20	5	80.00	1,273.68	3,198.09	-654.14	-1,290.24	1.95	7.79	888.11
6	22,151.30	25	21	4	84.00	1,189.00	3,147.85	-704.43	-1,500.88	1.69	8.86	886.05
5	18,930.44	25	20	5	80.00	1,095.50	2,353.88	-595.93	-1,077.30	1.84	7.35	757.22
4	16,165.00	25	18	7	72.00	1,161.24	3,173.92	-676.77	-1,024.50	1.72	4.41	646.60
3	8,799.96	25	16	9	64.00	889.56	2,227.50	-603.67	-978.00	1.47	2.62	352.00
2	9,940.07	25	16	9	64.00	956.93	2,314.87	-596.75	-1,562.33	1.60	2.85	397.60
1	5,448.70	25	16	9	64.00	617.08	2,073.34	-491.62	-1,393.26	1.26	2.23	217.95

The only instance not to close above the entry price in the next week triggered on 1/25/12. It took 7 trading days.

This suggests further upside is likely over the next 1-2 weeks. Below I have listed all the instances assuming an 8-day exit strategy.

SPX closes at a 100-day high on a Fed Day.
Buy on close. Sell X days later. $100k/trade. 1994 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
08/16/94	Buy	$465.01	1.89%	$2,072.60
08/26/94	Sell	$473.81		($763.25)
03/28/95	Buy	$503.90	0.50%	$841.50
04/07/95	Sell	$506.42		($1,623.60)
05/23/95	Buy	$528.58	1.33%	$1,729.35
06/05/95	Sell	$535.62		($1,360.80)
07/06/95	Buy	$553.99	0.81%	$1,611.00
07/18/95	Sell	$558.46		($169.20)
11/15/95	Buy	$593.96	2.10%	$2,098.32
11/28/95	Sell	$606.45		($73.92)
01/31/96	Buy	$636.01	4.00%	$4,229.58
02/12/96	Sell	$661.46		($361.10)
07/02/97	Buy	$904.05	2.40%	$2,431.00
07/15/97	Sell	$925.78		($172.70)
02/04/98	Buy	$1,006.90	1.58%	$2,090.88
02/17/98	Sell	$1,022.77		($656.37)
07/01/98	Buy	$1,148.56	2.53%	$2,714.40
07/14/98	Sell	$1,177.59		($484.59)
12/22/98	Buy	$1,203.56	3.42%	$3,755.75
01/05/99	Sell	$1,244.78		$0.00
06/30/99	Buy	$1,372.86	1.51%	$2,460.96
07/13/99	Sell	$1,393.56		($871.20)
11/16/99	Buy	$1,420.03	(0.86%)	$366.80
11/29/99	Sell	$1,407.83		($1,460.20)
12/21/99	Buy	$1,433.43	1.52%	$3,075.33
01/03/00	Sell	$1,455.22		($302.22)
03/21/00	Buy	$1,493.82	0.32%	$3,897.30
03/31/00	Sell	$1,498.58		($1,266.54)
05/06/03	Buy	$934.39	1.06%	$1,525.82
05/16/03	Sell	$944.30		($1,569.69)
12/14/04	Buy	$1,203.38	0.13%	$895.57
12/27/04	Sell	$1,204.92		($831.66)
10/25/06	Buy	$1,382.22	(0.18%)	$520.56
11/06/06	Sell	$1,379.78		($1,529.28)
05/09/07	Buy	$1,512.58	0.83%	$1,141.14
05/21/07	Sell	$1,525.10		($1,396.56)
03/16/10	Buy	$1,159.46	0.61%	$1,825.78
03/26/10	Sell	$1,166.59		($565.88)
11/03/10	Buy	$1,197.96	(0.02%)	$2,416.96
11/15/10	Sell	$1,197.75		($322.04)
12/14/10	Buy	$1,241.59	1.28%	$1,424.00
12/27/10	Sell	$1,257.54		($699.20)
01/26/11	Buy	$1,296.63	1.73%	$2,018.94
02/07/11	Sell	$1,319.05		($1,657.81)
04/27/11	Buy	$1,355.66	(0.69%)	$1,089.16
05/09/11	Sell	$1,346.29		($1,933.77)
01/25/12	Buy	$1,326.06	1.38%	$1,446.00
02/06/12	Sell	$1,344.33		($1,917.75)
03/13/12	Buy	$1,395.96	0.08%	$1,280.84
03/23/12	Sell	$1,397.11		($645.39)

The ***average*** run-up ($1,958) is bigger than the ***largest*** drawdown ($1,934).

In addition to the strong consistency, risk/reward also clearly favors the bulls. So the strong reaction on the news out of the Fed appears to be a good thing when the market is already locked in an uptrend.

But the Fed threw a little wrench in my works today. As I have been mentioning, POMO flows are currently in a short-term contraction. In fact, the QE Buying Power Swing System triggered short today as the QE Buying Power Index closed at 0. Below is a study based on similar parameters to the system.

QE Buying Power Index <= 0. SPX closes in top 20% of 10-day range.
Buy on close. Sell X days later. $100k/trade. 2008 - present.

QE POMO trade: daysin	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-40,088.18	40	17	23	42.50	948.55	2,386.98	-2,444.06	-4,932.90	0.39	0.29	-1,002.20
4	-37,415.33	45	20	25	44.44	1,061.61	2,044.02	-2,345.91	-6,578.61	0.45	0.36	-831.45
3	-25,035.49	52	23	29	44.23	981.26	4,441.44	-1,641.53	-4,353.44	0.60	0.47	-481.45
2	-39,477.96	66	30	36	45.45	768.63	3,811.00	-1,737.14	-9,986.13	0.44	0.37	-598.15
1	-41,785.59	109	51	58	46.79	557.71	4,063.35	-1,210.84	-8,883.33	0.46	0.41	-383.35

But now we have QE3. And what was looking like a temporary liquidity squeeze no longer appears so. Unfortunately (for our own tracking), the Fed is not using POMO to implement QE3. Instead of treasuries they are going to be buying agency mortgage backed securities. And it does not appear a schedule will be immediately ready, but it may be released in the near future. From the Fed's website:

How much will the Desk purchase each month in agency MBS associated with the reinvestment program and how will this be communicated?

On or around the eighth business day of each month, the Desk will publish a tentative amount of reinvestment-related purchases expected to take place between the middle of the current month and the middle of the following month. This amount will be approximately equal to the amount of principal payments from agency debt and agency MBS expected to be received over that period, adjusted for any variations from prior periods. Adjustments for any deviation between anticipated and actual agency MBS purchases over a given monthly period will be made by modifying the following month's agency MBS purchases. For example, if actual agency MBS purchases were $1 billion smaller (larger) than previously announced, the Desk would increase (decrease) the following month's anticipated agency MBS purchases by $1 billion.

I'll need to see what the schedule looks like when it is released (if it isn't already). My initial thought is simply to combine the two schedules to measure total flows. If anyone sees additional information on this please let me know. I will not be including the POMO study above on the Active list, since it may already be stale (or will likely be in a few days).

I have updated the Aggregator chart below.

The green Aggregator Line is again above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line dove sharply zero. This means the SPX is "overbought" versus recent expectations. So net expectations are bullish but the SPX is overbought. This is considered a neutral configuration. Neutral configurations are visible on the chart whenever both lines close on opposite sides of 0. This led the Aggregator to change from long to flat at the close, as was indicated as likely on the systems page before the bell.

Based on the current open studies, expectations are scheduled to remain positive on Friday. Of course this could change if more bearish evidence emerges. The Differential Pivot will be 1,435.30 on Friday. So it would take a close at or below this level in order to turn the SPX back to oversold.

Unfortunately I was too conservative with my entries on this Aggregator signal and I failed to take advantage of it. At this point I feel price is too extended to make new buys. I'll sit and wait for the next strong edge to avail itself.

Intermediate-term Outlook (2 weeks – 2 months)– updated 9/10– slightly bullish

The intermediate-term outlook was last updated in the 9/10 Subscriber Letter. A link may be found below.

2012-09-10 QE Subscriber Letter.pdf

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.

***None tonight*.**

Current Open Trade Ideas

None