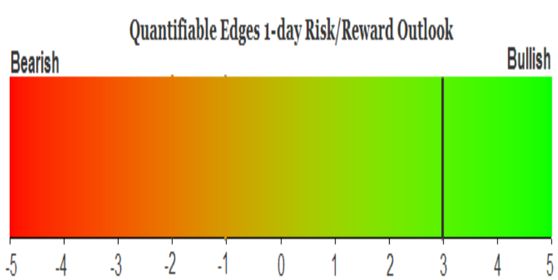
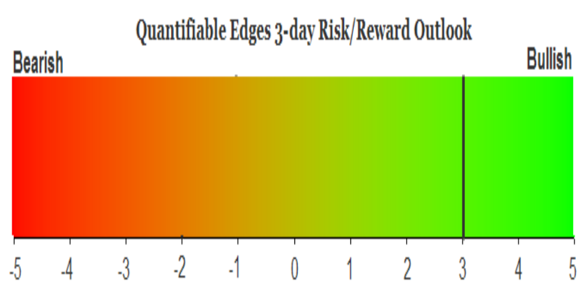
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

December 5, 2012 Volume 5 Issue 233

Market Overview





Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Long	100% Long XIV	Flat	Long

Tonight's Research Points

- SPY has closed at a 5-day for the 1st time in over 2 weeks. This suggests a short-term upside edge.

Short-term Outlook
The Bottom Line

Expectations are positive and the market is now oversold. I began scaling in at the close Tuesday. Several factors have me interested beginning a long XIV (inverse VIX ETN) position as well.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
December 5, 2012	1st 5 day low in 10 days	1-4 days	Bullish	1.60%
December 4, 2012	1 day dn after 5 up	1-5 days	Bullish	2.20%
December 3, 2012	VIX up SPX up Friday	1-3 days	Bearish	
November 27, 2012	1 day dn after 5 up	1-9 days	Bullish	2.10%
Active - Long Term				
December 3, 2012	Nasdaq leading SPX	int term	Bullish	
November 26, 2012	90% up vol studies.	1-15 days	Bullish	
November 19, 2012	CBI >= 11	1-20 days	Bullish	
October 15, 2012	Breadth not diverging at top	int term	Bullish	
September 17, 2012	QE3	int term	Bullish	
February 1, 2012	Golden Cross	int term	Bullish	

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

The Evidence

Trade was slow and mostly lower on Tuesday. The SPX and each Nasdaq fell 0.2%, but the Russell 2000 gained 0.2%. Breadth was slightly negative as the NYSE Up Issues % was 48% and the Up Volume % came in at 45%. Total NYSE volume was a little higher than Monday.

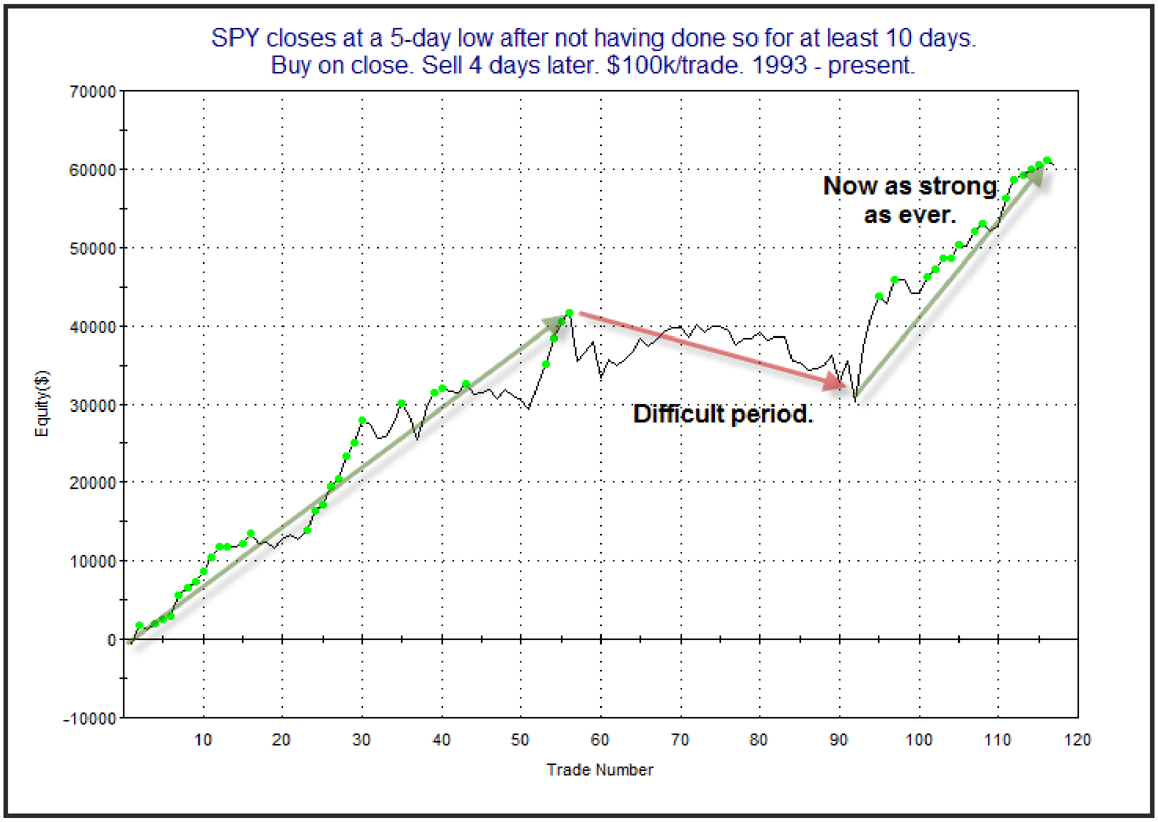
The market had gone without a pullback for a while. In the 8/24/12 subscriber letter I showed a study that examined results when the SPY closed at a 5-day low for the 1st time in over 2 weeks. It triggered again on Tuesday and I have updated it below.

SPY closes at a 5-day low after not having done so for at least 10 days.
Buy 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
10	95,397.70	117	78	39	66.67	2,189.48	8,925.10	-1,932.86	-8,623.54	1.13	2.27	815.36
9	81,355.82	117	78	39	66.67	1,973.60	8,933.76	-1,861.15	-6,709.56	1.06	2.12	695.35
8	76,171.41	117	77	39	65.81	1,918.00	8,908.38	-1,833.71	-7,113.48	1.05	2.07	651.04
7	61,633.49	117	76	41	64.96	1,849.67	6,851.52	-1,925.39	-7,790.40	0.96	1.78	526.78
6	49,119.55	117	75	42	64.10	1,644.60	6,523.92	-1,767.27	-9,559.44	0.93	1.66	419.83
5	47,505.24	117	72	44	61.54	1,616.64	6,103.89	-1,565.74	-4,906.44	1.03	1.69	406.03
4	60,294.75	117	78	39	66.67	1,439.69	6,941.43	-1,333.36	-6,244.56	1.08	2.16	515.34
3	37,171.53	117	72	45	61.54	1,312.86	5,888.16	-1,274.54	-5,295.84	1.03	1.65	317.71
2	23,391.83	117	65	51	55.56	1,131.68	3,809.72	-983.67	-3,737.28	1.15	1.47	199.93
1	12,791.74	117	65	52	55.56	852.73	2,812.20	-819.92	-3,909.03	1.04	1.30	109.33

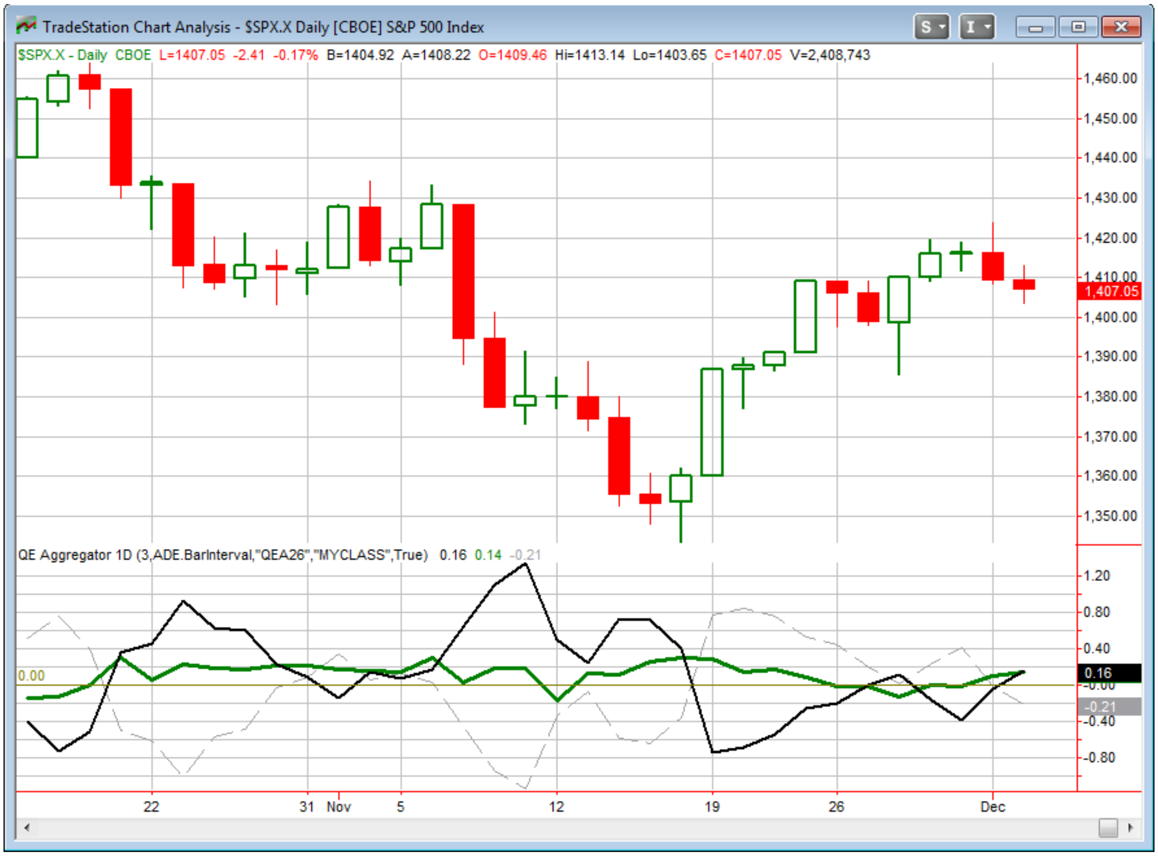
102 of 117 instances (87%) closed above the entry price
at some point in the next week.

Results here suggest a moderate upside edge. With the 4-day exit appearing to be compelling from a % Profitable, Avg Trade, and Profit Factor standpoint I ran an equity curve with it.



After showing a pretty consistent upside edge for nearly 60 instances, it chopped a bit. Over the last 25 trades or so the edge seems to have reasserted itself.

I have updated the Aggregator chart below.



With tonight's bullish study now included the green Aggregator line moved further above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line turned positive as well. This means the SPX is oversold versus recent expectations. So net expectations are bullish and the SPX is now oversold. This is considered a bullish configuration. Bullish configurations are visible on the chart whenever both lines close above 0. This caused the Aggregator system to turn from flat to long at the close.

Based on the current studies, expectations are set to remain positive on Wednesday. Of course this could change if bearish studies emerge. The Differential Pivot will be 1,414.13 on Wednesday. So to move from oversold to overbought the SPX will have to rise over 0.5%.

As anticipated, the Aggregator turned long at the bell. And when it did, I began to scale in to an index position. Rather than looking to put on a 2nd lot right away, I'm going to look to take a position in XIV (the inverse VIX ETF). I have not taken an XIV position in a couple of months, but it now appears to be a favorable time to do so. I say this for a few reasons.

1) Upside SPX edge – Evidence is suggesting we should see the SPX rally over the next few days. When SPX rallies VIX typically declines. So the upside market bias should aide an XIV position.
2) VIX is stretched upwards – The VIX is currently hitting multi-week highs and has risen 14% over the last 3 days. Its mean-reverting tendency is quite strong and if it pulls back, VIX futures most likely will as well, helping XIV.
3) VIX futures contango is fairly strong – Contango means that 2nd month VIX futures are currently quite a bit more expensive than front month. XIV rolls its future positions every day to maintain a constant maturity. This means each day it is shorting 2nd month futures and buying (to cover) front month futures at a lower price. This contango is currently 8.5%. Meaning XIV would benefit by 8.5% over the course of a month at the current level of contango. That is fairly sizable, especially considering the stretched VIX.

So the combination of all these factors has me quite interested in XIV at the moment. I'll look to take a partial position in it on Wednesday. Details are in the Trade Ideas section down below.

More on contango and how XIV works can be found on the videos page in the VIX-based ETF webinars.

To get a quick view of the VIX futures term structure at any time I'd suggest http://vixcentral.com/

I also recommend Bill Luby's work over at http://vixandmore.blogspot.com/ who discusses these issues on a regular basis.

Intermediate-term Outlook (2 weeks – 2 months)– updated 12/3– bullish

The intermediate-term outlook was last updated in the 12/3/12 letter. Link below:

2012-12-03 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.

XIV buy 1/2 XIV position @ $18.48 LIMIT. Based on the short-term outlook above.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	12/4/2012	$141.25	$141.25	0.00%		bought on close