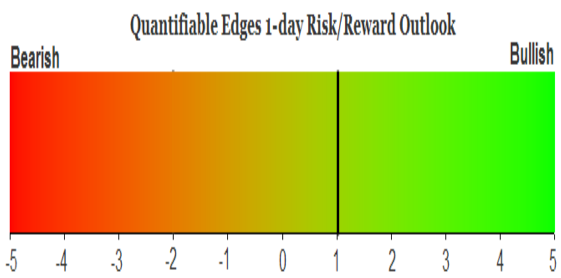
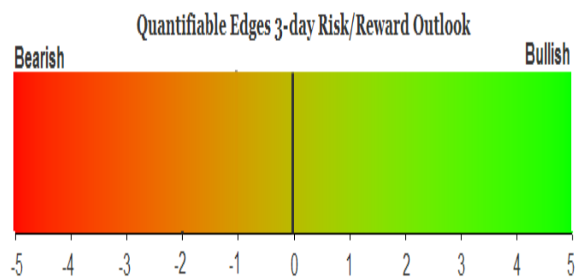
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

December 13, 2012 Volume 5 Issue 239

Market Overview





Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Short	100% Short SPY	Flat	Flat

Tonight's Research Points

- Short-term highs on a Fed Day are often met by a pullback over the next few days.
- SPX hitting a 10-day high while the VIX also rises tends to lead to wekness the next day.

Short-term Outlook

The Bottom Line

Evidence has turned bearish again and the SPX is overbought. While that would normally indicate a short-side edge, the QE Buying Power Index remains strong. And the bearish evidence is very short-lived. So I'm not inclined to short here, but an aggressive, nimble traders could have a downside edge to take advantage of.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
December 13, 2012	VIX up SPX 10-high MidWeek	1 day	Bearish	
December 13, 2012	10-Day Hig on Fed Day	1-2 days	Bearish	
December 12, 2012	5 days up > 200ma & < 50-high	1-10 days	Bullish	2.00%
Active - Long Term				
December 12, 2012	5 days up > 200ma & < 50-high	1-15 days	Bullish	2.80%
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	
Dropped Tonight				
December 11, 2012	VIX up SPX 10-high Monday	1-2 days	Bearish	

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

The Evidence

Wednesday was strong for most of the day, but most profits were given back late in the day. The SPX ended with a 0.04% gain while the NASDAQ fell 0.3%, and the Russell 2000 lost 0.7%. Breadth was mixed as the NYSE Up Issues % was 43% and the Up Volume % came in at 56%. Total NYSE volume rose came in just slightly below Tuesday's level.

As most subscribers are no doubt aware, the VIX and the SPX will most often move opposite each other. But on Wednesday they both closed up. In the 11/23/12 Letter I showed one study that suggested a possible downside edge for the next day. Below I have updated the stats.

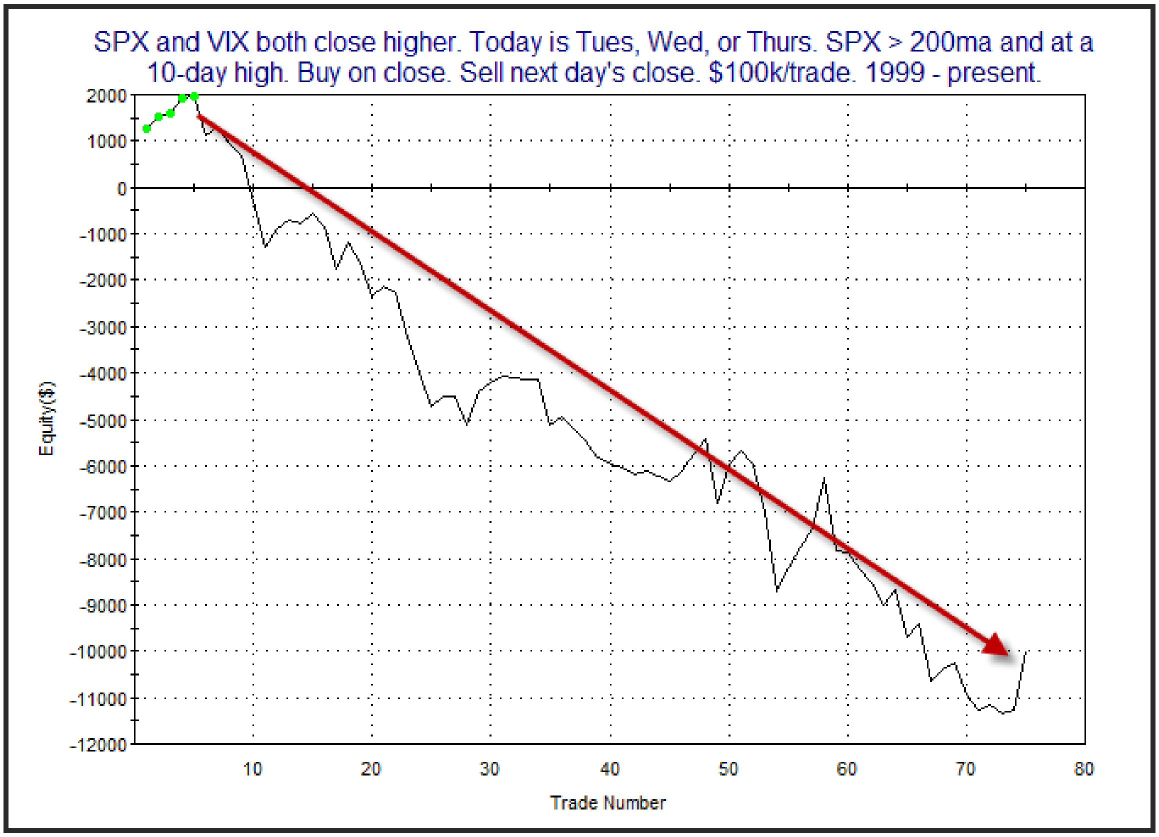
SPX and VIX both close higher. Today is Tues, Wed, or Thurs. SPX > 200ma and at a 10-day high. Buy on close. Sell next day's close. $100k/trade. 1999 - present.

TradeStation Performance Summary Collapse

All Trades

Total Net Profit	($9,975.61)	Profit Factor	0.55
Gross Profit	$12,208.61	Gross Loss	($22,184.22)
Total Number of Trades	75	Percent Profitable	45.33%
Winning Trades	34	Losing Trades	41
Even Trades	0		
Avg. Trade Net Profit	($133.01)	Ratio Avg. Win:Avg. Loss	0.66
Avg. Winning Trade	$359.08	Avg. Losing Trade	($541.08)
Largest Winning Trade	$1,286.52	Largest Losing Trade	($1,721.70)

Numbers here suggest a mild downside inclination. They are good enough to take a look at the profit curve.



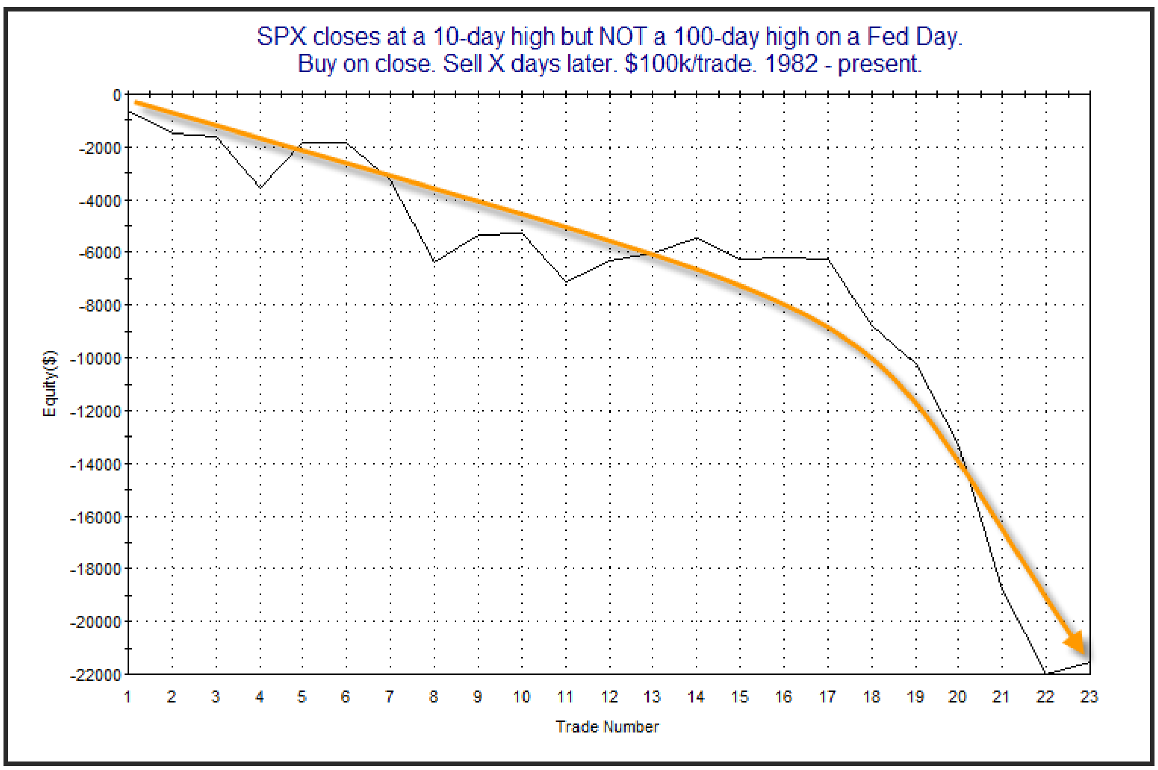
The steady downslope here is impressive despite the big jump on the last instance. I have therefore elected to include this study on the Active List.

When the SPX is not also making a long-term high, then moves to new short-term highs often get reversed over the next few days. (Long-term highs are another story for another day.) This is exemplified by the study below, which was last seen in the 3/17/10 Letter.

SPX closes at 10-day high BUT NOT 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: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	-22,428.25	23	10	13	43.48	1,621.06	-2,972.22	0.55	0.42	-975.14
9	-26,627.76	23	10	13	43.48	1,582.23	-3,265.39	0.48	0.37	-1,157.73
8	-21,076.00	23	10	13	43.48	1,323.16	-2,639.05	0.50	0.39	-916.35
7	-10,459.04	23	12	11	52.17	1,725.71	-2,833.42	0.61	0.66	-454.74
6	-11,454.63	23	11	12	47.83	1,556.71	-2,381.54	0.65	0.60	-498.03
5	-22,916.76	23	9	14	39.13	1,524.38	-2,616.87	0.58	0.37	-996.38
4	-20,034.37	23	9	14	39.13	1,146.14	-2,167.83	0.53	0.34	-871.06
3	-13,125.70	23	11	12	47.83	1,372.39	-2,351.83	0.58	0.53	-570.68
2	-21,554.72	23	8	15	34.78	626.38	-1,771.05	0.35	0.19	-937.16
1	-12,017.71	23	6	17	26.09	924.91	-1,033.36	0.90	0.32	-522.51

22 of 23 instances (96%) closed below the Fed Day close at some point in the next 4 days.

The numbers here all point to a downside edge, primarily over the 1st 2 days. Below is a profit curve showing how the edge has played out over time.



Not the smoothest curve, but I prefer a steepening one like this to a flattening one. I think this study is compelling enough to include on the Active List.

I have updated the Aggregator chart below.

The studies tonight caused the green Aggregator line to cross back below 0. Negative readings mean net expectations from the Active List are for downside over the next few days. Meanwhile the black Differential Line is still in negative territory. This means the SPX is overbought versus recent expectations. So net expectations are negative and the SPX is overbought. This is considered a bearish configuration. Bearish configurations are visible on the chart whenever both lines close below 0. This caused the Aggregator system to turn from flat to shorr at the close.

Based on the current studies, expectations are set to turn back to bullish on Thursday. Of course this could easily change if more bearish studies emerge. The Differential Pivot will be 1,422.23 on Thursday. This is about 0.4% below Wednesday's close. So the SPX will need to close down at least this much in order to move from overbought to oversold.

Evidence is pointing lower, but like a couple of days ago the downside edge appears to be short-lived. A short could be taken by a nimble trader, but I'm not inclined to try it this time. While the Aggregator is bearish the QE Buying Power Index is still at 3. So liquidity is flush. Over the last 5 years or so trying to short when the QE Buying Power Index was this strong has been a very difficult task.

While the Aggregator short signal may be short lived, I am not inclined to fight it with the current XIV position. VIX futures contango has weakened. It is now about 6.5% for the front 2 months. If we get a pullback in the SPX over the next few days, there is a good chance we could re-enter the XIV trade at a better price. Risk is high right now with the directional edge gone and the contango edge reduced. So I'll look to get flat and then re-assess over the next few days. Details are in the Trade Ideas section at the bottom of the Letter.

Intermediate-term Outlook (2 weeks – 2 months)– updated 12/10– bullish

The intermediate-term outlook was last updated in the 12/10 Letter. Link below:
2012-12-10 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

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
XIV(1/2)	12/5/2012	$18.48	$19.13	3.52%		sell @ $19.00 limit

I'll look to sell XIV at a price of $19.00 or higher. If it opens below $18.50, I will lower my limit to $18.50. If it opens between $18.50 an $19.00, I'll use $18.50 as my stop and still use $19.00 as my limit price.