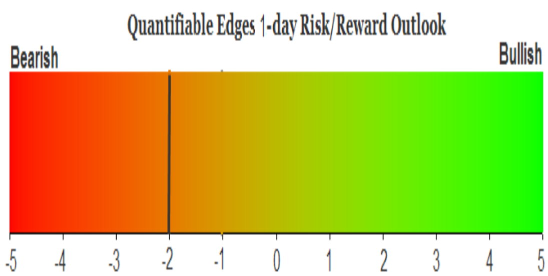
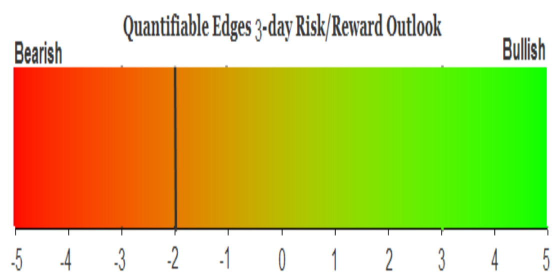
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 25, 2013 Volume 6 Issue 57

Market Overview





Signals Overview

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

Tonight's Research Points

- Unfilled gaps up that fail to make a higher high will often pull back over the next few days.
- Holy Thursday has been mostly positive over the last 32 years.

Short-term Outlook

The Bottom Line

The Aggregator is now suggesting a short-term downside edge. But the weakness is only expected to last a very short time, and with liquidity still so strong, I am not inclined to try and short.

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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				
March 25, 2013	Inside day. Lower high. Close>open.	1 day	Bearish	
March 22, 2013	Unfill gap up then gap dn	1-3 days	Bearish	
March 20, 2013	3 down from 50 < 10ma > 10-low	1-4 days	Bullish	1.80%
March 19, 2013	2 unfilled gaps dn. 5-low. Close>200.	1-5 days	Bullish	1.80%
March 18, 2013	Unfill gap up then gap dn from 20-hi.	1-7 days	Bearish	-2.20%
Active - Long Term				
March 13, 2013	5 days up to 50-high, then 1 down	1-10 days	Bullish	2.00%
January 14, 2013	Breadth Divergence (from Tops Study)	int term	Bearish	
September 17, 2012	QE3	int term	Bullish	
February 1, 2012	Golden Cross	int term	Bullish	
Dropped Tonight				
March 21, 2013	Gap-n-go on a Fed Day	1-2 days	Bearish	-1.40%
March 20, 2013	3 dn. Tomorrow Fed Day	1-3 days	Bullish	2.00%
March 19, 2013	1st 5-day low in over 2 weeks	1-4 days	Bullish	1.60%

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

The Evidence

The market reversed direction for the 3rd day in a row as Friday saw gains. The SPX and Nasdaq each gained 0.7% and the Russell 2000 rose 0.25%. Breadth was squarely positive as the NYSE Up Issues % was 63% and the Up Volume % came in at 66%. Total NYSE volume fell for the 3rd day in a row.

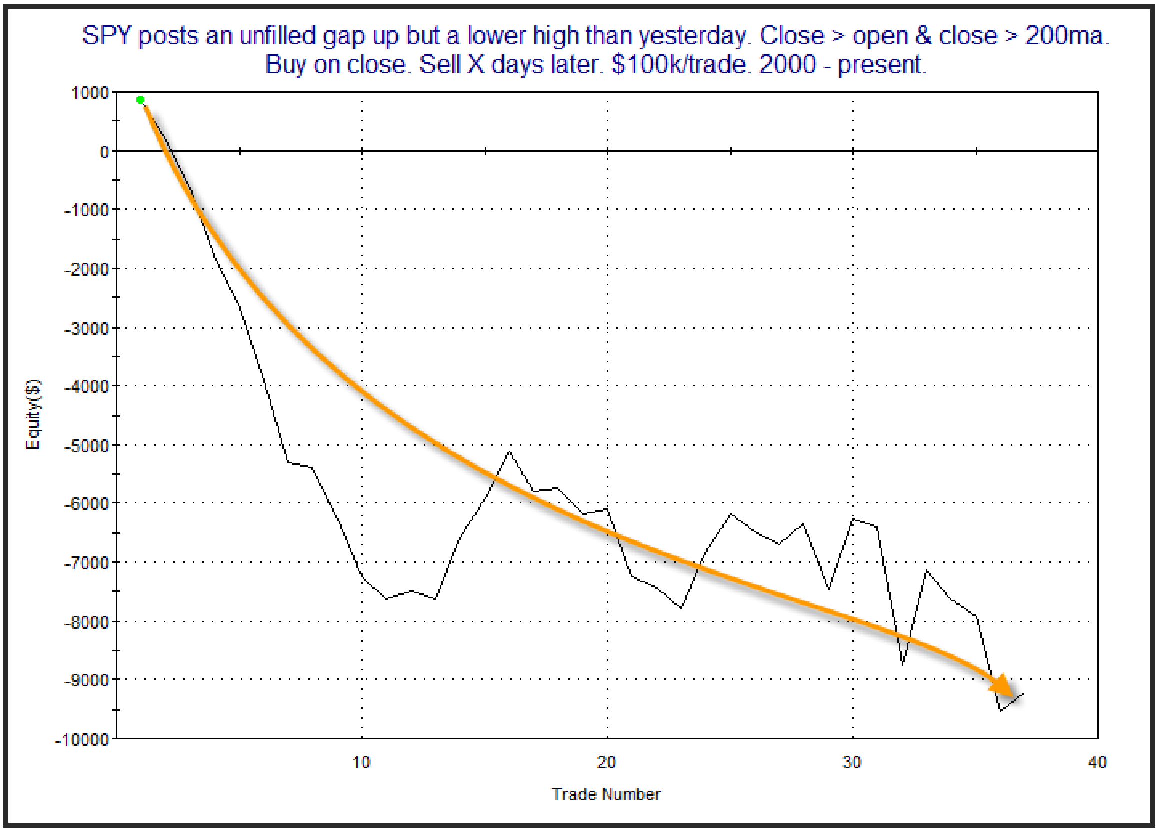
Friday's action was unusual in that not only was it an inside day, but it also posted an unfilled gap up. In the 6/25/12 letter I looked at days like Friday where the market gapped higher, never filled, and moved higher from open to close without making a higher high. I've updated those results below.

SPY posts an unfilled gap up but a lower high than yesterday. Close > open & close > 200ma.
Buy on close. Sell X days later. $100k/trade. 2000 - 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
5	-8,112.83	35	15	20	42.86	1,392.59	2,556.33	-1,450.09	-3,477.70	0.96	0.72	-231.80
4	-9,806.19	35	16	19	45.71	1,161.94	1,964.02	-1,494.59	-7,544.70	0.78	0.65	-280.18
3	-10,618.24	36	16	20	44.44	871.86	2,311.02	-1,228.40	-6,150.30	0.71	0.57	-294.95
2	-9,536.92	37	13	24	35.14	937.23	1,859.92	-905.04	-2,929.90	1.04	0.56	-257.75
1	-9,201.15	37	13	24	35.14	676.34	1,600.62	-749.73	-2,348.90	0.90	0.49	-248.68

32 of 37 instances (86%) closed below the entry price
at some point in the next week.

Implications here appear somewhat bearish, with most of the damage occurring on day 1. Below is a profit curve that shows how the downside edge has played out over time.



This is not an ideal profit curve but it still appears to suggest a downside edge. Without much else new to go on tonight I felt it was worth giving this study some consideration.

We do have a strong seasonal day coming up this week that I should note. Last year in the 4/5/12 Subscriber Letter I showed how the SPX has performed strong on Holy Thursday, which is the Thursday before Easter. Friday the market is closed and it is not unusual for the market to exhibit a bullish bias heading in to a long weekend. (President's Day is the lone exception that comes to mind without a bullish bias ahead of it.) I've updated the study below which shows how the SPX has performed over the last 32 years on Holy Thursday.

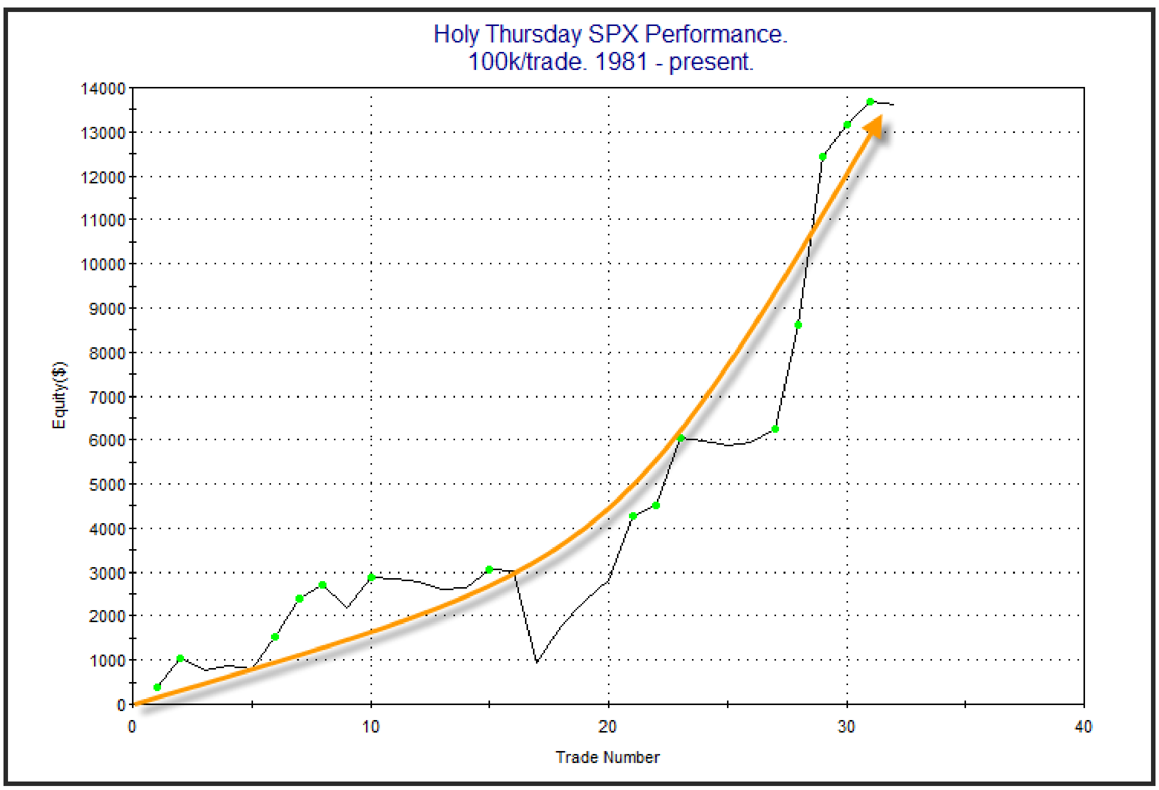
Holy Thursday SPX Performance.
100k/trade. 1981 - present.

TradeStation Performance Summary

All Trades

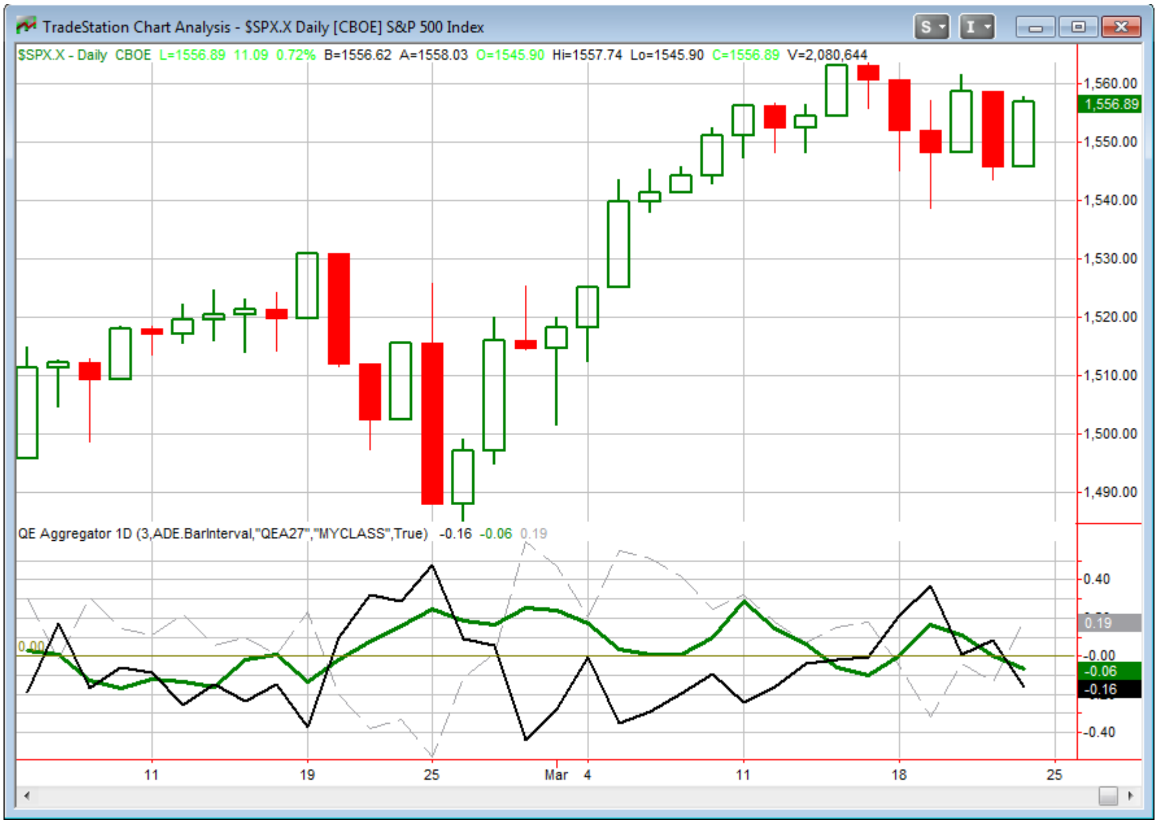
Total Net Profit	$13,630.35	Profit Factor	4.90
Gross Profit	$17,125.46	Gross Loss	($3,495.11)
Total Number of Trades	32	Percent Profitable	65.63%
Winning Trades	21	Losing Trades	11
Even Trades	0		
Avg. Trade Net Profit	$425.95	Ratio Avg. Win:Avg. Loss	2.57
Avg. Winning Trade	$815.50	Avg. Losing Trade	($317.74)
Largest Winning Trade	$3,799.40	Largest Losing Trade	($2,097.90)

The numbers are compelling, and it is especially impressive to see how much the winners have outsized the losers. Below is the profit curve.



The upward bias has been in effect the whole period but the SPX has performed even better more recently. Last year did not manage to close higher, but SPX only declined less than 1 point.

I have updated the Aggregator chart below.



With the short-term studies now leaning bearish the green Aggregator Line dipped down below zero. Negative readings mean net expectations from the Active List are for downside over the next few days. Meanwhile the black Differential Line also fell below 0. The negative Differential Line reading means the SPX is now overbought versus recent expectations. So expectations are bearish 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 change from long to short at the close.

Based on the current short-term studies, expectations are set remain bearish on Monday. Of course this could easily change if more bullish evidence emerges. The Differential Pivot will be *inverted at* 1,562.96 on Monday. This is *0.4% above* Monday's close. An inverted pivot means the Differential Line would move through 0 if SPX closes flat. So for the SPX to remain overbought it is going to need to rise at least 0.4%.

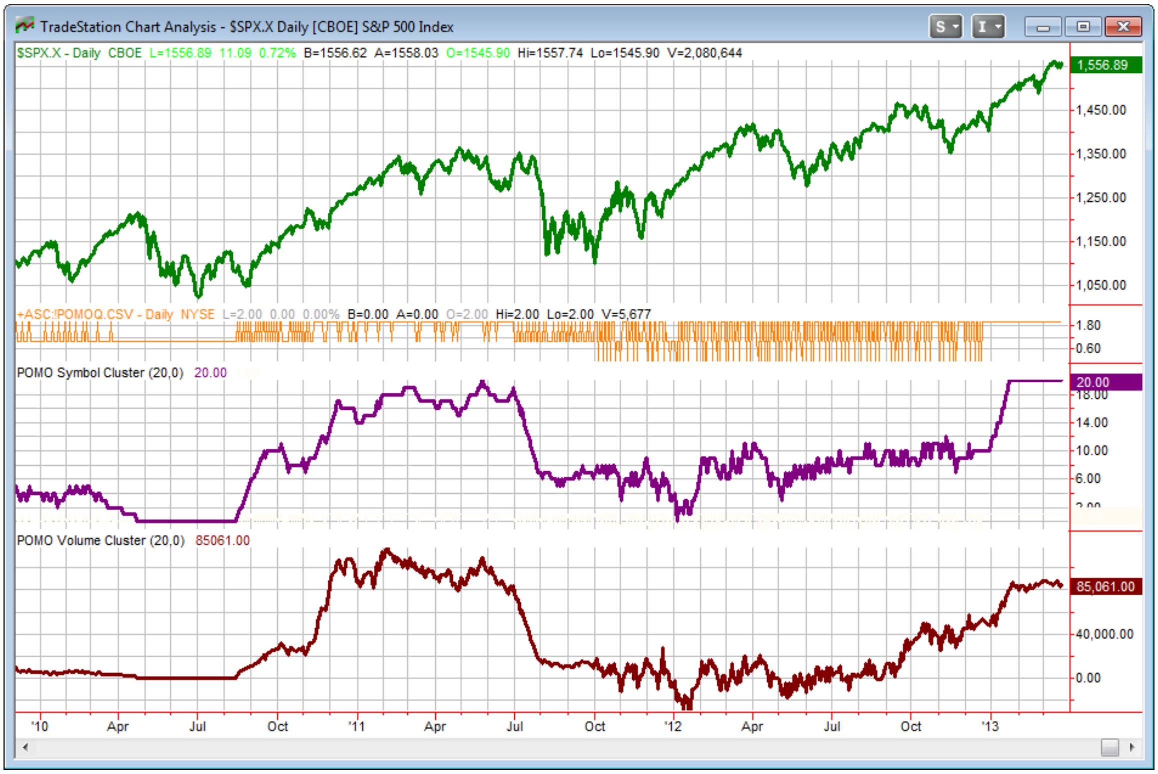
Inverted pivots mean the opportunity to profit is limited. If the market goes in the anticipated direction then the short signal will close out in 1 day. So I sometimes don't take new trade signals that occur with an inverted pivot. Of course I'm still not inclined to short since the QE Buying Power Index remains so strong. So I am not looking to take on any additional exposure right now, but will wait and see how things play out and what studies emerge over the next few days.

Intermediate-term Outlook (2 weeks – 2 months)– updated 3/25 – bullish

The market chopped around this week and failed to close up on the week for only the 2nd time in 2013. Of course the damage was limited, with the SPX pulling back a mere 4 points. The choppy action failed to inspire any new studies with intermediate-term implications.

I update the intermediate-term POMO/QE chart each week. For those not familiar, below is a brief description.

POMO stands for Permanent Open Market Operations and it is how the Fed has gone into the open market to buy securities over the last several years. 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 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. Since the Sept 13, 2012 QE3 announcement the POMO numbers are also adjusted to reflected the Fed's new approach of buying AMBS securities. Therefore, prior to that date the indicators just look at POMO, since that date it is a combination of POMO and AMBS flows.



The POMO/AMBS volume indicator remained elevated in its 2013 range again this week. And the days indicator is ***still*** maxed out at 20, which was a rarity during past QE implementations, but has been the norm so far this year. We estimate net inflows this past week to have been about $19.75 billion. That is again a strong week. Numbers like this normally provide a nice bullish wind at the market's back in the following days.

This upcoming week is also expected to see strong liquidity. Between POMO and AMBS we should see about a $18.9 billion inflow. While that is a little less than this past week, it will be accomplished in only 4 days, since Friday is a holiday. The liquidity environment continues to be one that is favorable for the bulls.

The POMO & AMBS schedules for April are due to come out on Thursday. There was no change in policy announced at the Fed meeting this past week, so we expect to see similar liquidity provided next month. The link below will take you to the POMO schedule, which will be updated around 1pm on Thursday.

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

Of course next weekend I will use it to generate the anticipated QE Buying Power Index values for April, and will share any observations I have about the schedule.

Overall, intermediate-term evidence is mixed but leaning positive. On the negative side we are still cognizant of the breadth divergence from the Study of Tops (available on the members download page). But liquidity and momentum are both positive and they have been difficult to bet against, even short-term, in 2013. Until I see more evidence of a change in trend I'll continue to favor the long side.

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

Open Catapult Triggers

GOOG – 1/3 @ $807.79 (filled)

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 1(GOOG)

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)	***3/18/2013***	***$22.02***	***$22.35***	***1.50%***		***stopped out intraday***
GOOG(1/3)	3/19/2013	$807.79	$810.15	0.29%		Catapult
BRF	3/22/2013	$40.38	$40.00	-0.94%		Bought @ limit