

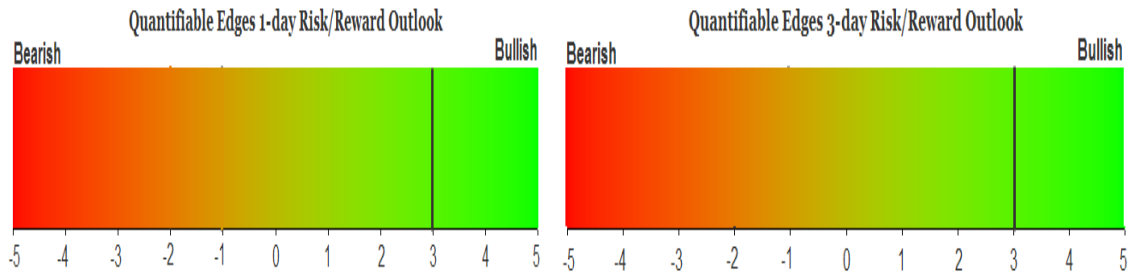
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 6, 2014

Volume 7 Issue 25

Market Overview



Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing
Long	75% Long XIV	Long

Tonight's Research Points

- The CBI reached 10 on Wednesday for the first time since 2012. Historically, readings this high have been reliable indications that a bounce is near.

Short-term Outlook

The Bottom Line

I still like the long side for the short-term, and more Catapults triggered on Wednesday that will allow me to potentially benefit from a rally.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active - Short Term				
February 6, 2014	CBI > 10. SPX > 200ma.	1-4 days	Bullish	1.70%
February 5, 2014	Sweet Spot bounce	1-5 days	Bullish	2.90%
February 4, 2014	Strong drop to int-low. Close > 200	1-5 days	Bullish	
February 4, 2014	VIX 100-high. SPX > 100-low	1-7 days	Bullish	
February 3, 2014	End of Month < 10ma and > 200ma	1-5 days	Bullish	2.20%
January 31, 2014	20-low then sideways chop	1-5 days	Bullish	
Active - Long Term				
January 27, 2014	2 unfilled dn gaps & 5-low > 200	1-10 days	Bullish	
December 23, 2014	QE Tapering	int term	Neutral	
December 18, 2013	4 Hindenburg Triggers	1 - 35 days	Bearish	-7.00%
December 2, 2013	Nasdaq leading SPX	int term	Bullish	
October 21, 2013	70% Advancing Issues 3 Days In Row	1-75 days	Bullish	10.60%
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish	
February 1, 2012	Golden Cross	int term	Bullish	
Dropped Tonight				
January 30, 2014	20-low on a Fed Day	1-5 days	Bullish	2.10%

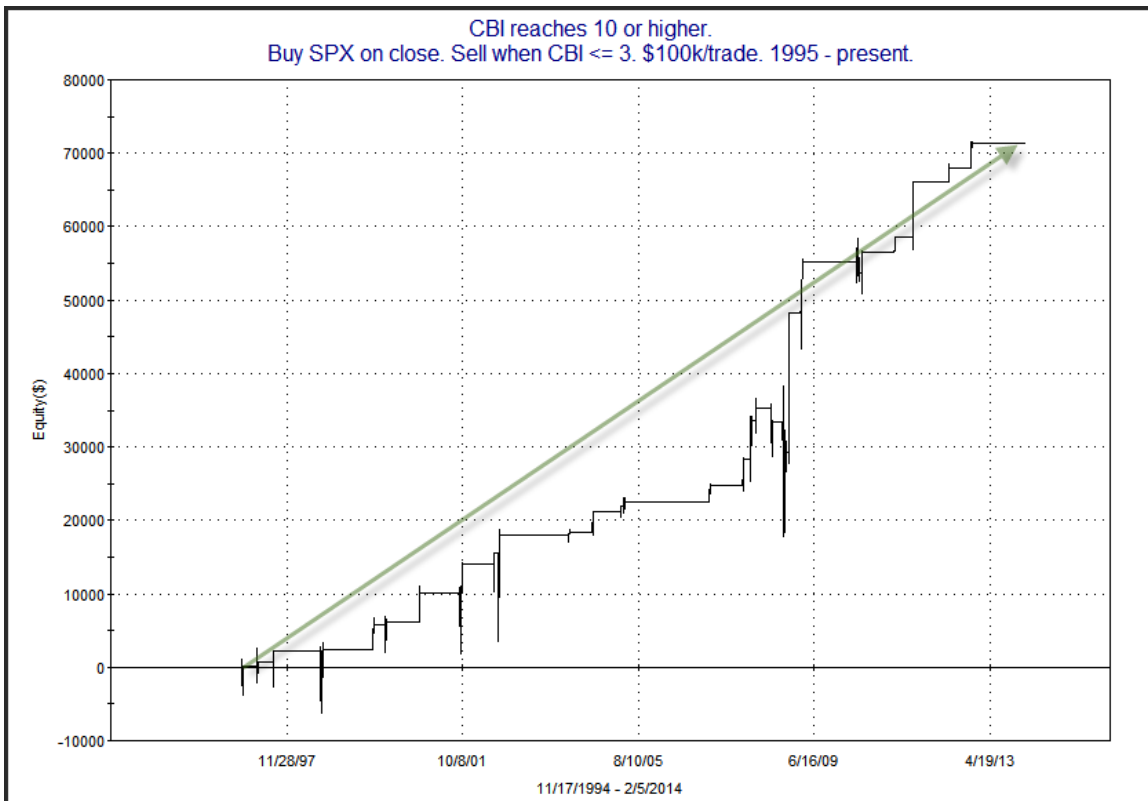
The Evidence

After some strong selling in the morning, the market turned around and actually made it positive in the afternoon. But late selling left the indices all lower. The SPX lost 0.2%, the Nasdaq fell 0.5% and the Russell 2000 declined 0.8%. Breadth was negative as the NYSE Up Issues % came in at 39% and the Up Volume % was 43%. Total NYSE volume fell for the 2nd day in a row.

The relatively mild down finish on Wednesday failed to trigger any Quantifinder studies. But we did see one of our indicators post a notably extreme reading. That's the Quantifiable Edges Capitulative Breadth Indicator (CBI). The CBI is simply a raw count of the number of Catapult triggers that are active at any one time. As many subscribers are aware, high CBI readings have generally meant there is a broad number of stocks that are undergoing extreme selling, and are primed for a bounce. When a fair number of stocks are primed for a bounce, that has also translated into the market itself enjoying a short-term rally. In the past I have [shown a fair amount of research](#) demonstrating CBI levels of 10 or greater have generally been enough to lead to a market rally within a few short days. One simple strategy I have shown in the past that could take advantage of a high CBI is to purchase SPX when the CBI reaches 10 or higher, and then exit this trade when the CBI gets back down to 3 or lower. CBI history is available back to 1995 (and Quantifiable Edges subscribers may download it directly from the [Catapult System page](#)). Results below show how this strategy would have performed from 1995 - present.

CBI reaches 10 or higher. Buy SPX on close. Sell when CBI <= 3. \$100k/trade. 1995 - present.			
TradeStation Performance Summary			Collapse ^
All Trades			
Total Net Profit	\$71,407.77	Profit Factor	10.44
Gross Profit	\$78,968.49	Gross Loss	(\$7,560.72)
Total Number of Trades	28	Percent Profitable	89.29%
Winning Trades	25	Losing Trades	3
Even Trades	0		
Avg. Trade Net Profit	\$2,550.28	Ratio Avg. Win:Avg. Loss	1.25
Avg. Winning Trade	\$3,158.74	Avg. Losing Trade	(\$2,520.24)
Largest Winning Trade	\$18,981.60	Largest Losing Trade	(\$4,214.00)

As you can see, results have strongly favored the bulls. A very high percentage of the instances would have led to winning trades, and overall gains have swamped overall losses by over 10x. Below is a profit curve that shows how this strategy would have played out over time.



While individual trades have seen dips, the end results have generally been strong, and there has not been a period of time in which the curve appeared to be rolling over.

But selling is not as extreme now as it was in many of the instances seen over time. Personally, I have found that relatively strong selloffs during long-term uptrends are substantially different than relatively strong selloffs during long-term downtrends. In other words, CBI readings > 10 have occurred under different conditions and led to different kinds of rallies depending on whether the market was trading above or below its 200ma. Below I have broken out the strategy results based on whether the setup triggered while SPX was above or below its 200ma.

CBI reaches 10 or higher. SPX < 200ma.
Buy SPX on close. Sell when CBI <= 3. \$100k/trade. 1995 - present.

TradeStation Performance Summary Collapse ^			
All Trades			
Total Net Profit	\$61,412.00	Profit Factor	9.12
Gross Profit	\$68,972.72	Gross Loss	(\$7,560.72)
Total Number of Trades	19	Percent Profitable	84.21%
Winning Trades	16	Losing Trades	3
Even Trades	0		
Avg. Trade Net Profit	\$3,232.21	Ratio Avg. Win:Avg. Loss	1.71
Avg. Winning Trade	\$4,310.80	Avg. Losing Trade	(\$2,520.24)
Largest Winning Trade	\$18,981.60	Largest Losing Trade	(\$4,214.00)

CBI reaches 10 or higher. SPX > 200ma.
Buy SPX on close. Sell when CBI <= 3. \$100k/trade. 1995 - present.

TradeStation Performance Summary Collapse ^			
All Trades			
Total Net Profit	\$9,995.77	Profit Factor	n/a
Gross Profit	\$9,995.77	Gross Loss	\$0.00
Total Number of Trades	9	Percent Profitable	100.00%
Winning Trades	9	Losing Trades	0
Even Trades	0		
Avg. Trade Net Profit	\$1,110.64	Ratio Avg. Win:Avg. Loss	n/a
Avg. Winning Trade	\$1,110.64	Avg. Losing Trade	\$0.00
Largest Winning Trade	\$2,338.56	Largest Losing Trade	\$0.00

As you can see, instances above the 200ma have been more reliable, but less powerful. The average bounce under these circumstances is just over 1%. And the largest winning trade was a little over 2.3%. But the average trade when below the 200ma has been 3.2%. This is larger than the largest below the 200ma, and nearly 3x the average. So I believe it is important to make this distinction when setting expectations for the bounce over the next few days. Below is a listing of all 9 previous instances above the 200ma.

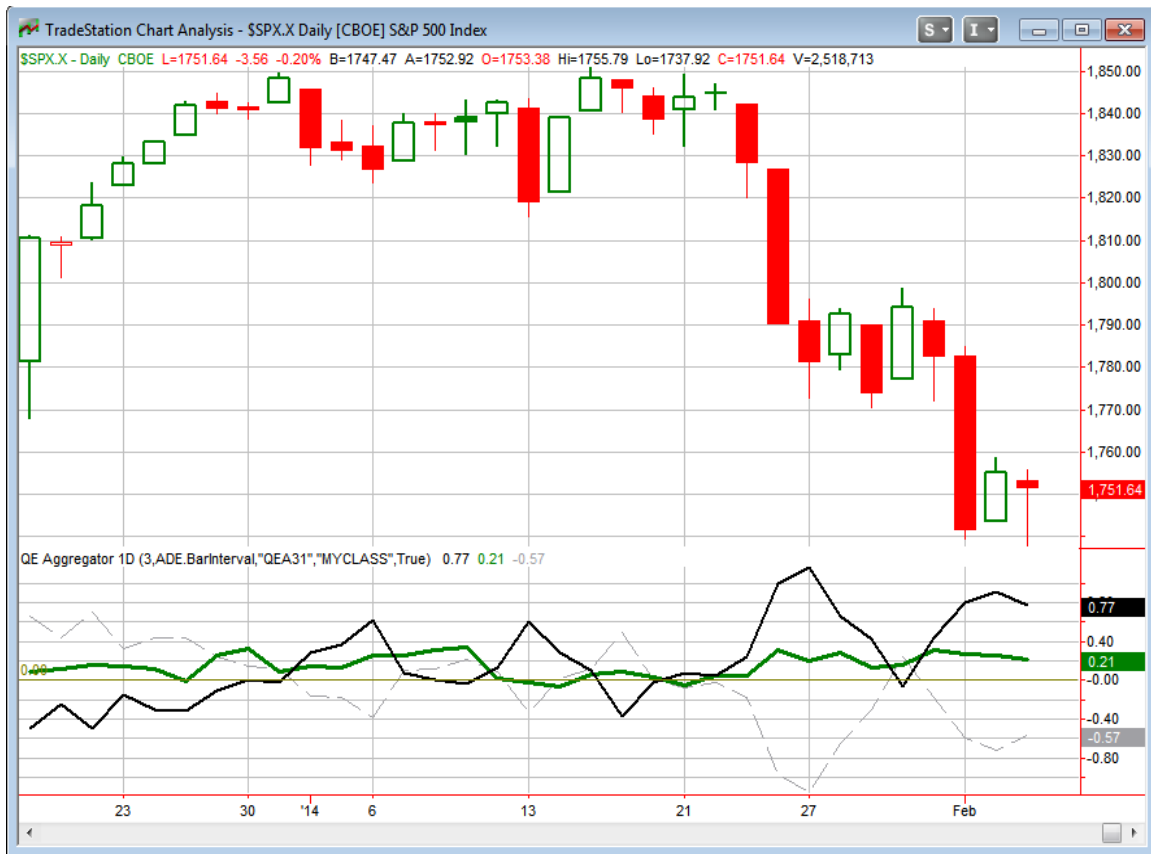
CBI reaches 10 or higher. SPX > 200ma. Buy SPX on close. Sell when CBI <= 3. \$100k/trade. 1995 - present.				
Date/Time	Signal	Price	% Profit	Run-up Drawdown
12/04/96	Buy	\$745.10	0.09%	\$1,116.22
12/19/96	Sell	\$745.77		(\$3,806.94)
04/03/97	Buy	\$750.32	0.59%	\$2,554.93
04/15/97	Sell	\$754.72		(\$2,231.74)
08/14/97	Buy	\$924.77	1.58%	\$1,574.64
08/20/97	Sell	\$939.35		(\$3,394.44)
01/26/00	Buy	\$1,404.09	0.37%	\$1,048.67
02/01/00	Sell	\$1,409.28		(\$3,836.84)
02/02/04	Buy	\$1,135.26	0.40%	\$809.60
02/09/04	Sell	\$1,139.81		(\$952.16)
03/23/05	Buy	\$1,172.53	0.76%	\$765.85
03/30/05	Sell	\$1,181.41		(\$751.40)
03/05/07	Buy	\$1,374.12	2.36%	\$2,594.16
03/12/07	Sell	\$1,406.60		\$0.00
03/17/11	Buy	\$1,273.72	1.94%	\$2,095.08
03/21/11	Sell	\$1,298.38		\$0.00
05/18/12	Buy	\$1,295.22	1.97%	\$2,561.79
05/24/12	Sell	\$1,320.68		\$0.00

While the bounces have not been as strong, the drawdown has been much more controlled under these circumstances. The largest drawdown so far has been less than 4%. Lastly, let's take a peek at returns on a time basis rather than looking to simply exit on a reduction of the CBI.

CBI reaches 10 or higher. SPX > 200ma. Buy SPX on close. Sell X days later. \$100k/trade. 1995 - 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	8,833.00	9	8	1	88.89	1,177.32	2,803.32	-585.58	-585.58	2.01	16.08	981.44
4	10,939.07	9	9	0	100.00	1,215.45	2,068.56	0.00	0.00	100.00	100.00	1,215.45
3	6,360.98	9	6	3	66.67	1,373.23	2,101.40	-626.13	-683.73	2.19	4.39	706.78
2	624.89	9	5	4	55.56	1,315.08	1,923.48	-1,487.63	-3,119.03	0.88	1.11	69.43
1	1,465.15	9	5	4	55.56	927.26	1,599.29	-792.78	-2,587.68	1.17	1.46	162.79

In the past the edge has primarily played out over the next four days. I have added CBI spikes to the Short-Term Active List tonight.

I have updated the [Aggregator](#) chart below.



The high CBI reading helped keep the green Aggregator Line squarely above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. We also saw the black Differential Line again close strongly above 0. The positive Differential Line reading means the SPX is oversold versus recent expectations. So expectations are positive and the SPX is oversold. This is considered a bullish configuration. Bullish configurations are visible on the chart whenever both lines close above 0. This caused the Aggregator signal to remain long.

Based on the current open studies, expectations are slated to remain positive on Thursday. The Differential Pivot will be 1754.56 on Thursday. That is just about three points above Wednesday's close. This is because Monday's extra-large drop is going to be falling off the back of the Differential calculation. So it won't take much of a rally on Thursday for SPX to move from oversold to overbought and the Differential Line to cross down below zero.

I'm still of the opinion that the market is likely to see a short-term rally occur in the next few days. And we have seen a multitude of bullish evidence over the last few days to support that opinion. Under most circumstances I would be aggressively buying a CBI reading of 10. But since the Differential Pivot is so close by, I decided instead that I will

look to add to my index position near the close. There were three new Catapults that triggered on Wednesday, so I will be taking on more exposure through those purchases early in the day (if I receive fills). Details are in the Trade Ideas section down below.

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

The intermediate-term outlook was last updated in the 2/3 Letter. It can be found in the most recent weekly letter on the website.

<http://quantifiableedges.com/current-weekly-letter/>

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

Open Catapult Triggers

COF – 1/3 @ \$69.95(bought @ limit)

FCX – 1/3 @ \$31.08 (buy @ limit)

COP – 1/3 @ \$63.86 (buy @ limit)

NWSA – 1/3 @ \$15.52 (buy @ limit)

FCX – 1/3 @ \$30.94 (bought @ limit) – 2nd lot

COP – 1/3 @ \$63.71 (bought @ \$63.52) – 2nd lot

NWSA – 1/3 @ \$15.52 (no fill-cancel order for now)

New

TGT – 1/3 @ \$55.07 (buy @ limit) – 1st lot

COP – 1/3 @ \$63.46 (buy @ limit) – 3rd lot

CVX – 1/3 @ \$109.52 (buy @ limit) – 1st lot

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 10/6(COF, FCX-2, COP-3, NWSA-2, TGT, CVX)

Additional New Trade Ideas

A full listing of system triggers can be found at the [numbered systems 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.

TGT – buy 1/3 Catapult position @ \$55.07 LIMIT. This is a catapult system trigger. More about the Catapult System and CBI can be found in the recently updated Catapult & CBI presentation on [the Videos page](#) or on the [Catapult System page](#).

COP – buy 1/3 Catapult position @ \$63.46 LIMIT. This is a catapult system trigger from the Catapult & CBI section above. This will be the 3rd lot for COP.

CVX – buy 1/3 Catapult position @ \$109.52 LIMIT. This is a catapult system trigger from the Catapult & CBI section above. This will be the 1st lot for CVX.

SPY – buy ¼ index position @ \$175.00 LIMIT ON CLOSE. Based on the short-term outlook above and the high CBI reading. I will look to take on a third lot of SPY if it fails to rally much on Thursday.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	1/27/2014	\$178.89	\$174.87	-2.25%		Aggregator
SPY(1/4)	1/27/2014	\$178.01	\$174.87	-1.76%		Aggregator
COF(1/3)	1/28/2014	\$69.95	\$68.66	-1.84%		Catapult
FCX(1/3)	2/4/2014	\$31.08	\$31.09	0.03%		Catapult
NWSA(1/3)	2/4/2014	\$15.52	\$15.61	0.58%		Catapult
COP(1/3)	2/4/2014	\$63.86	\$63.46	-0.63%		Catapult
FCX(1/3)	2/5/2014	\$30.94	\$31.09	0.48%		Catapult
COP(1/3)	2/5/2014	\$63.52	\$63.46	-0.09%		Catapult

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