

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 5, 2014

Volume 7 Issue 167

Market Overview



Signals Overview

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

Tonight's Research Points

- 3-day pullbacks with a low 3/10 Offset HV suggest a bullish edge.
- The first drop below the 10ma in quite a while will often be followed by another leg up.

Short-term Outlook

The Bottom Line

The Aggregator is still bullish. And with SPX closing down 3 days in a row now, I am interested in starting to scale in to a long position.

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

Study Date	Description	Time span	Bias	Avg Run-up	Avg DrawDn	Avg DrawDn - 1 Std Dev
Active - Short Term						
September 5, 2014	1st close < 10ma in > 15 days	1-3 days	Bullish			
September 5, 2014	3 days down, 3/10 HV < 0.25	1-3 days	Bullish			
September 2, 2014	End of month at high of month	1-5 days	Bullish			
September 2, 2014	Labor Day week after 4-week rise	1-4 days	Bearish	-1.50%	1.20%	2.20%
Active - Long Term						
September 4, 2014	SPX 20-day high, NDX biggest loss in 20	1-50 days	Bullish	6.50%	-2.70%	-5.10%
August 22, 2014	50-low to 50-high in 2 weeks	1-17 days	Bullish	5.40%	0.90%	-1.90%
August 20, 2014	SPX RSI(2) crosses over 99	1-15 days	Bullish	2.40%	-1.50%	-2.90%
June 2, 2014	NASDAQ leading SPX	int term	Bullish			
April 28, 2014	Sell in May	6 months	Bearish			
December 23, 2013	QE Tapering	int term	Neutral			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			
February 1, 2012	Golden Cross	int term	Bullish			

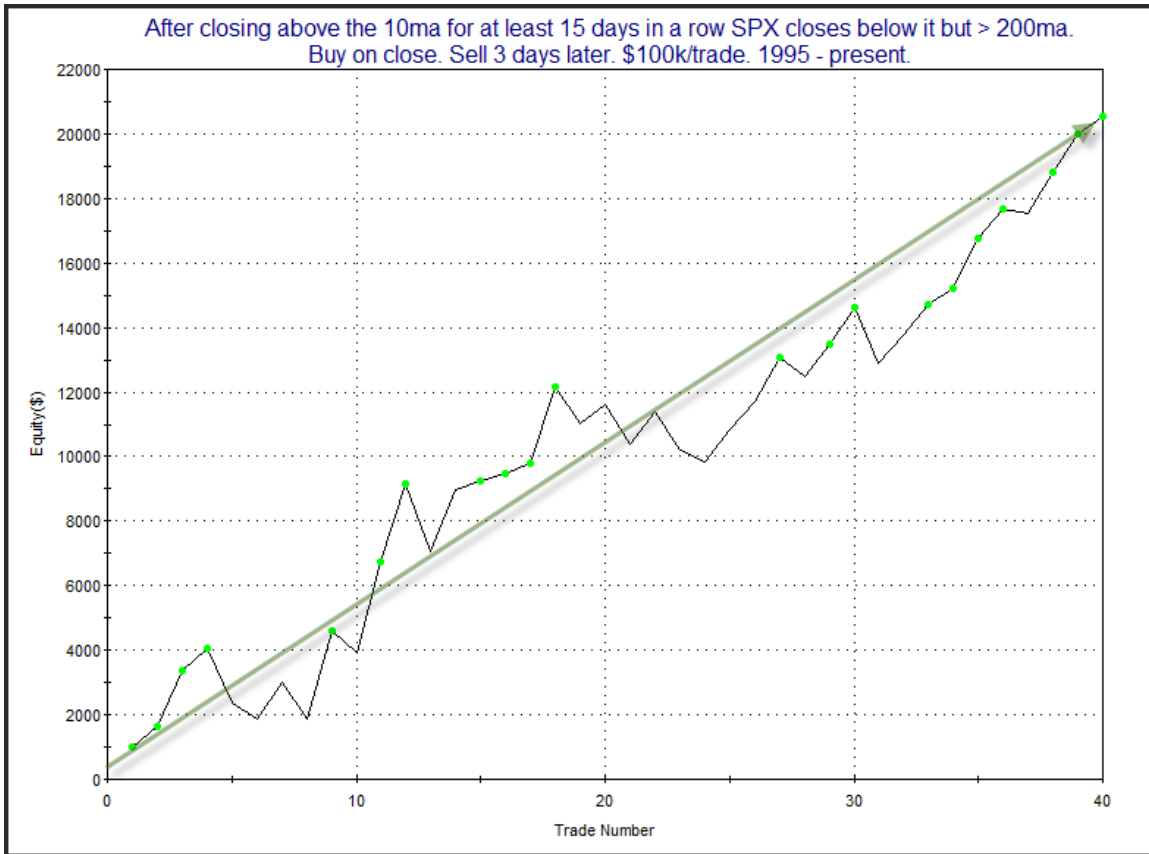
The Evidence

In a pattern that keeps playing out this week a strong morning was followed by an afternoon fade. The SPX and NASDAQ finished down 0.2% while the Russell 2000 fell 0.4%. Breadth was negative as the NYSE Up Issues % came in at 34% and the Up Volume % was 39%. Total NYSE volume rose a little from Wednesday's level.

The persistent uptrend of late has kept SPX above its short-term moving averages for an extended period. I pointed this out over the last few days and indicated that I was not inclined to take a long position until SPY/SPX pulled back a bit. Thursday, after 17 consecutive closes above the 10ma, SPX sliced down and closed a little below it. SPY meanwhile closed just a hair above its 10ma. In the 3/14/14 letter I looked at performance following other instances where SPX closed below its 10ma for the first time in a while. Results are updated below.

After closing above the 10ma for at least 15 days in a row SPX closes below it but > 200ma. Buy 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	30,334.20	48	30	18	62.50	1,571.58	3,505.74	-934.07	-2,959.70	1.68	2.80	631.96
4	29,298.13	48	33	15	68.75	1,413.60	3,206.40	-1,156.70	-3,078.40	1.22	2.69	610.38
3	23,305.06	48	33	15	68.75	1,148.55	2,805.12	-973.14	-2,062.10	1.18	2.60	485.52
2	13,286.23	48	29	19	60.42	1,103.16	2,682.72	-984.49	-2,185.60	1.12	1.71	276.80
1	12,334.26	48	28	20	58.33	769.84	2,097.92	-461.07	-1,542.24	1.67	2.34	256.96
42 of 48 instances (87.5%) closed above the entry price at some point in the next week.												

The numbers here all look solidly bullish over the next week. I highlighted the 3-day holding period because it had a more appealing equity curve than the four or five-day. You can see its profit curve below.



The strong upslope serves as some confirmation of the bullish edge.

Another positive about the SPX pullback over the last 3 days is that the 3/10 Offset HV Indicator is extremely low. As a brief review the 3/10 Offset HV compares the current 3-day historical volatility to the historical volatility of the 10 days prior to these three. When very low readings occur that means there has been a sharp contraction in volatility. This often leads to a volatility expansion. It isn't often useful in determining direction. It does suggest that a large move could occur, though. The 0.25 level is one I tend to use. Historically it has reached 0.25 or lower about 9% of the time. The 3 days following such low readings have seen the 3-day HV expand 5.5 times over the next 3 days. A chart of the indicator can be found on the Quantifiable Edges charts page.

So let's take a look and see how the market has reacted following 3-day pullbacks with low readings vs. those without low readings. I last did this in the 11/21/13 letter and have updated the studies below. First I'll show times when the 3/10 Offset HV is above 0.25.

SPX closes down for exactly 3rd day in a row and HV Offset 3/10 indicator > 0.25.
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
10	46,813.83	124	72	52	58.06	2,877.64	10,849.26	-3,084.16	-16,890.72	0.93	1.29	377.53
9	70,006.20	129	78	51	60.47	2,707.92	12,144.60	-2,768.86	-15,942.36	0.98	1.50	542.68
8	54,756.31	132	79	52	59.85	2,636.06	12,293.93	-2,951.77	-14,092.68	0.89	1.36	414.82
7	62,700.41	139	79	60	56.83	2,604.52	12,277.87	-2,384.27	-9,109.80	1.09	1.44	451.08
6	42,933.72	142	79	63	55.63	2,308.14	10,326.58	-2,212.84	-11,683.62	1.04	1.31	302.35
5	52,622.81	152	80	72	52.63	2,391.33	9,830.18	-1,926.16	-18,000.90	1.24	1.38	346.20
4	53,947.81	160	95	65	59.38	1,865.57	7,119.69	-1,896.63	-17,037.90	0.98	1.44	337.17
3	38,998.73	160	92	68	57.50	1,630.37	7,687.63	-1,632.29	-10,286.10	1.00	1.35	243.74
2	29,638.31	160	91	69	56.88	1,375.57	7,249.63	-1,384.62	-9,270.00	0.99	1.31	185.24
1	38,306.40	160	97	63	60.63	1,044.04	6,901.83	-999.46	-3,810.60	1.04	1.61	239.41

As we knew from past studies there is a mild upside bias after a 3-day pullback. It appears over the last 14 years that the edge has really only lasted 1-day. Returns after the 1st day are fairly flat.

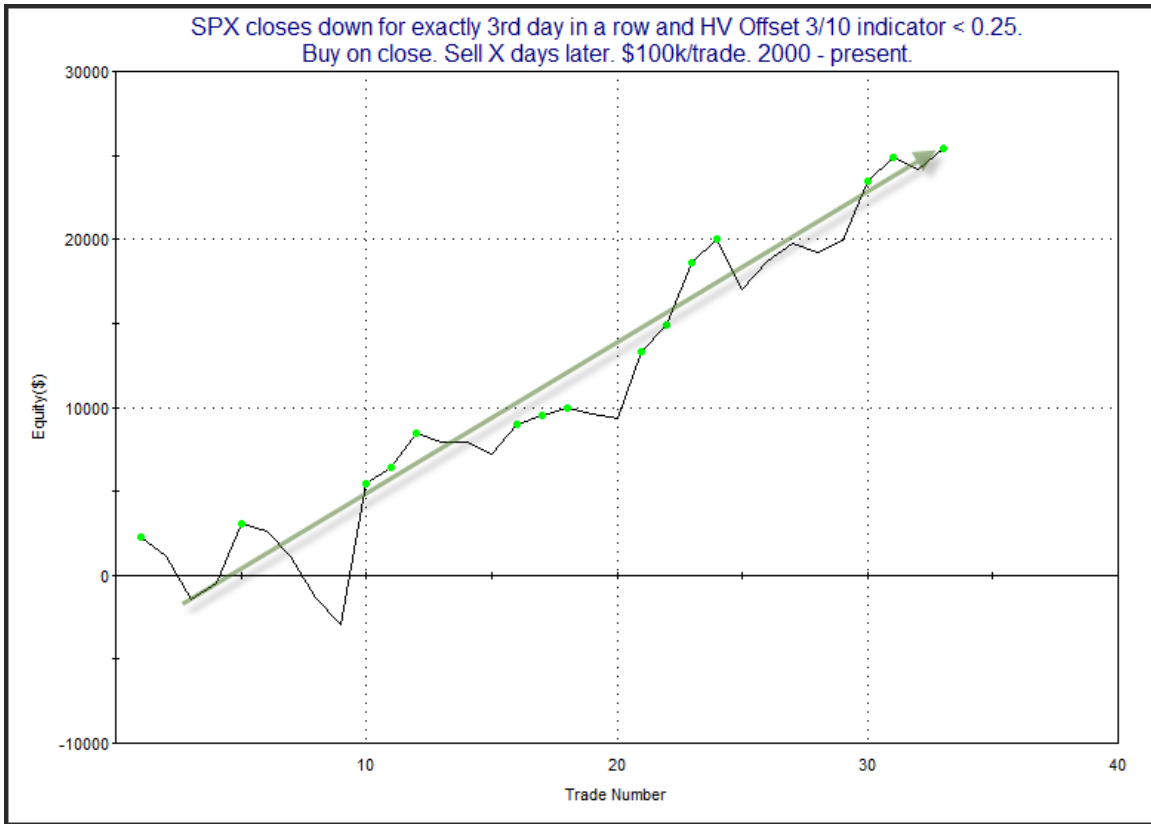
Now let's look at times like now where the 3/10 Offset HV is very low.

SPX closes down for exactly 3rd day in a row and HV Offset 3/10 indicator < 0.25.
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
10	34,937.82	32	21	11	65.63	2,779.79	13,815.90	-2,130.70	-5,143.04	1.30	2.49	1,091.81
9	33,158.38	32	21	11	65.63	2,495.74	11,206.23	-1,750.20	-5,817.60	1.43	2.72	1,036.20
8	30,901.25	32	21	11	65.63	2,635.76	11,382.35	-2,222.71	-4,624.64	1.19	2.26	965.66
7	17,979.50	32	19	13	59.38	2,491.91	10,117.38	-2,258.99	-5,582.08	1.10	1.61	561.86
6	20,225.23	33	20	13	60.61	2,538.33	5,903.59	-2,349.34	-7,964.16	1.08	1.66	612.89
5	24,904.51	33	21	12	63.64	2,426.95	8,234.80	-2,171.78	-7,032.56	1.12	1.96	754.68
4	19,460.57	33	21	12	63.64	2,144.83	8,810.76	-2,131.74	-7,145.44	1.01	1.76	589.71
3	25,370.99	33	19	14	57.58	2,166.61	8,432.34	-1,128.19	-3,021.92	1.92	2.61	768.82
2	21,064.51	33	20	13	60.61	1,780.62	5,018.23	-1,119.06	-5,271.36	1.59	2.45	638.32
1	7,718.10	33	20	13	60.61	982.37	2,971.43	-917.63	-4,660.72	1.07	1.65	233.88

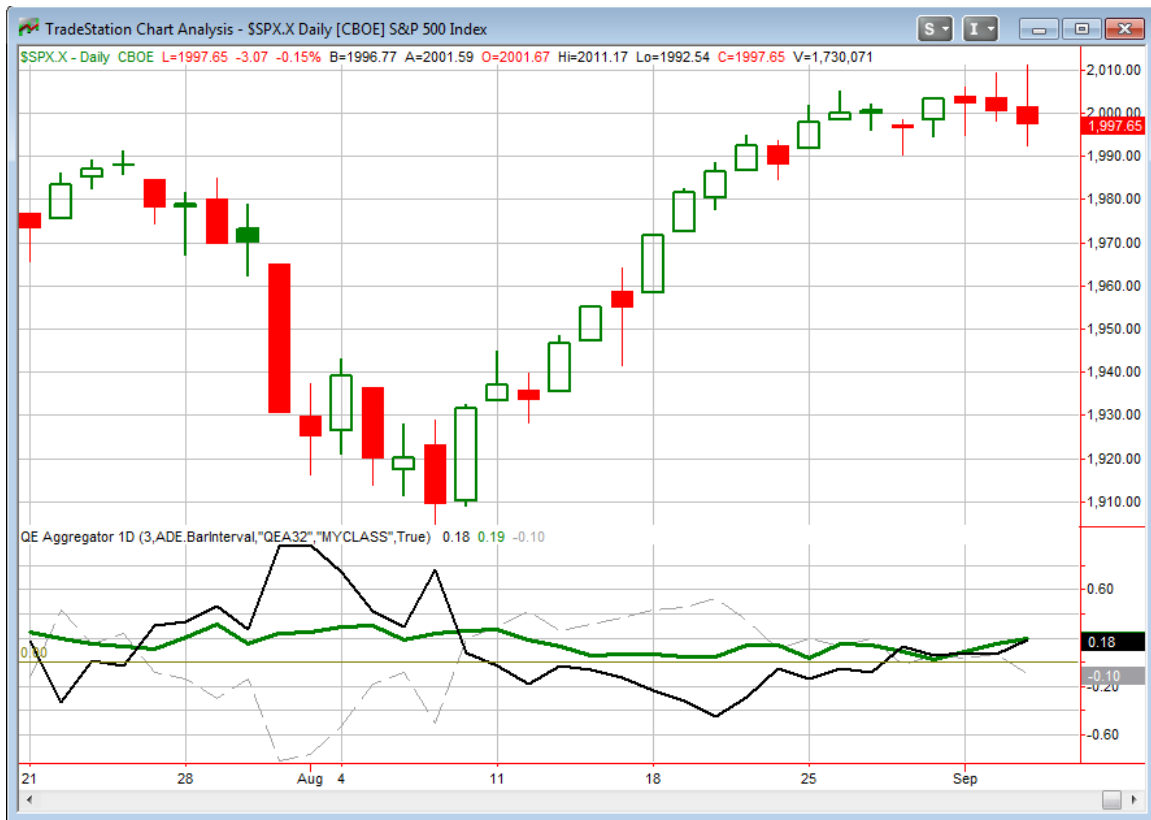
29 of 33 instances (88%) closed above the entry price at some point in the next week.

These numbers appear to be quite a bit better - both immediately and after a couple of weeks. The reliability of some kind of bounce improves nicely as well. Below is a profit curve assuming a 3-day exit strategy.



The strong upslope appears to confirm the stats table. The current pullback certainly contains some appealing characteristics.

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



With 2 new bullish studies being added tonight the green Aggregator Line managed rise a little 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 also held 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. Therefore the Aggregator signal stayed long at the close.

Expectations are set to remain positive on Friday. Of course this could easily change if strong new bearish evidence emerges. The Differential Pivot will be 2006.29 on Friday. That is 0.4% above Thursday's close. So for SPX to move from oversold to overbought it is going to need to close up at least 0.4% on Friday

I've ignored the bullish signal for a few days now with SPX having avoided a pullback for so long. This one is not yet very deep, but SPX has closed lower 3 days in a row now, and it also closed just below its 10ma. With short-term evidence all pointing higher and the market in a bit of a pullback, I will look to start scaling in long if I can get a favorable fill. Details are in the Trade Ideas section down below.

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

The intermediate-term outlook was last updated in the 8/25/14 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

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 [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.

SPY – buy ¼ index position @ \$200.21 LIMIT ON OPEN. If not filled, cancel order and then look to buy at \$200.21 LIMIT ON CLOSE. I would like to get a favorable fill here, so I will be looking to buy into either a gap down open or a lower close. I will not be a buyer of an intraday selloff. With the HV 3/10 Offset so low, and the employment report due out before the open, we could see a strong intraday move. And if the move is a gap up that starts heading lower, then I do not want to step in front of it.

Current Open Trade Ideas

None

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