

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

December 3, 2014

Volume 7 Issue 229

Market Overview



Signals Overview

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

Tonight's Research Points

- A 2nd Hindenburg Omen signal triggered on Tuesday. 3-4 signals have sometimes led to market difficulty in the past.

Short-term Outlook

The Bottom Line

The bounce on Tuesday arrived as anticipated. But it also nearly brought the market back to short-term overbought. Expectations remain positive and the rally seems primed to continue. But with the market nearly overbought again the reward/risk for new entries does not appear great.

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						
December 2, 2014	1st day under 10ma in over 25 days	1-4 days	Bullish	1.90%	-0.30%	-0.60%
December 1, 2014	Big drop from 50-day high	1-4 days	Bullish			
Active - Long Term						
December 2, 2014	1st day under 10ma in over 25 days	1-20 days	Bullish	4.74%	-0.35%	-0.65%
November 19, 2014	RSI2 > 99	1-10 days	Bullish			
November 18, 2014	SPX 3-high. Russell dn 3 in row	1-10 days	Bullish			
November 3, 2014	Best 6 Months	6 months	Bullish			
November 3, 2014	Quantitative Easing Ends	int term	Bearish			
October 27, 2014	NASDAQ leading SPX	int term	Bullish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			
February 1, 2012	Golden Cross	int term	Bullish			
Dropped Tonight						
December 2, 2014	System 11111	1-4 days	Bullish			

The Evidence

As the studies last night anticipated, the stock market bounced back nicely on Tuesday. The SPX and NASDAQ each rose 0.6%, and the Russell 2000 rallied 1.25%. Breadth was positive as the NYSE Up Issues % came in at 66% and the Up Volume % was 57%. Total NYSE volume sank a little from Monday's level.

The market was strong from open to close, which was a bit of a disappointment for the trade idea in last night's letter, because SPY fell \$0.03 shy of getting filled before taking off to the upside. The unfilled gap also meant that System 11111 did not trigger an entry. It has therefore been removed from the Short-Term Active List tonight.

The Quantifinder did note that a Hindenburg Omen signal triggered for the 2nd day in a row. Two signals has not been a reliable indication in the past. Generally, I look for 3-4 signals in order to even take Hindenburgs under consideration. I last discussed the Hindenburg Omen in detail in the 12/18/13 letter. I have copied that discussion below.

The Hindenburg Omen was created by Jim Miekka in 1995. It looks to identify times when there is a split market developing, which could signal trouble ahead. Tuesday marked the 4th recent Hindenburg Omen signals (under the less strict rules).

Below are the rules for a Hindenburg Omen signal.

- 1. The daily number of NYSE new 52 week highs and the daily number of new 52 week lows are both greater than or equal to 2.8 percent (typically about 84) of the sum of NYSE issues that advance or decline that day (typically, around 3000). The original version of the indicator used 2.2%. When I originally researched the Hindenburg Omens a few years ago, 2.2% was the number I used, and it is the number I again use in the studies below. (Two side notes: 1) If I use 2.8% rather than 2.2% there have only been 6 instances since 1980 where there has been a cluster of 3 or more triggers. Five saw lower prices ahead, but this does not give us a sample size that is really workable. 2) Over time I have also seen published different places levels of 2.4% and 2.5%, so there is often some confusion over this requirement.)*
- 2. The NYSE index is greater in value than it was 50 trading days ago. Originally, this was expressed as a rising 10 week moving average, but the new rule is more relevant to the daily data used to look at new highs and lows.*
- 3. The McClellan Oscillator is negative on the same day.*
- 4. New 52 week highs cannot be more than twice the new 52 week lows (though new 52 week lows may be more than double new highs).*

It is generally viewed that a single Hindenburg Omen signal is not a reliable indication of a market top, but that numerous signals provide a more reliable indication of danger. This is something I explored in the past and updated today. So let's look at some numbers. This first table shows results of entering the market when the 1st signal triggers.

Buy SPX when the 1st Hindenburg Omen triggers.
Sell X days later. \$100/trade. 1980 - 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
100	16,561.43	24	13	11	54.17	6,820.92	13,171.60	-6,555.51	-19,079.85	1.04	1.23	690.06
95	18,339.00	25	14	11	56.00	6,707.64	17,946.48	-6,869.81	-22,416.88	0.98	1.24	733.56
90	2,137.27	25	13	12	52.00	6,683.88	15,961.92	-7,062.76	-20,572.65	0.95	1.03	85.49
85	16,396.78	26	14	12	53.85	7,588.99	16,670.24	-7,487.42	-21,465.22	1.01	1.18	630.65
80	749.70	26	13	13	50.00	7,252.72	16,583.84	-7,195.06	-21,552.30	1.01	1.01	28.83
75	238.30	26	14	12	53.85	6,490.78	14,501.70	-7,552.72	-22,917.59	0.86	1.00	9.17
70	-5,136.07	26	12	14	46.15	7,937.35	17,714.32	-7,170.31	-20,289.64	1.11	0.95	-197.54
65	-15,707.93	26	12	14	46.15	7,324.52	16,609.84	-7,400.16	-21,508.76	0.99	0.85	-604.15
60	-31,054.88	26	12	14	46.15	6,303.86	17,197.44	-7,621.52	-24,323.31	0.83	0.71	-1,194.42
55	-55,722.66	26	11	15	42.31	5,941.98	14,306.24	-8,072.29	-27,246.71	0.74	0.54	-2,143.18
50	-35,732.04	26	10	16	38.46	6,738.56	14,509.04	-6,444.85	-29,846.67	1.05	0.65	-1,374.31
45	-22,085.93	27	13	14	48.15	5,422.72	13,151.98	-6,612.95	-23,971.88	0.82	0.76	-818.00
40	-19,862.13	27	12	15	44.44	6,092.06	12,520.58	-6,197.79	-23,520.93	0.98	0.79	-735.63
35	-19,328.91	29	13	16	44.83	5,817.65	12,021.20	-5,934.89	-24,659.19	0.98	0.80	-666.51
30	-11,643.85	29	15	14	51.72	4,624.67	9,855.58	-5,786.70	-22,460.42	0.80	0.86	-401.51
25	-5,947.21	30	14	16	46.67	5,152.84	9,781.64	-4,880.44	-27,340.01	1.06	0.92	-198.24
20	-10,929.02	31	16	15	51.61	3,949.12	9,257.67	-4,941.00	-19,533.91	0.80	0.85	-352.55
15	6,233.45	34	16	18	47.06	3,225.92	9,103.68	-2,521.18	-8,166.80	1.28	1.14	183.34
10	-3,262.76	40	19	21	47.50	2,522.20	9,012.33	-2,437.36	-7,899.90	1.03	0.94	-81.57
5	-20,127.73	50	17	33	34.00	1,849.17	4,926.56	-1,562.53	-5,775.12	1.18	0.61	-402.55

The numbers here certainly aren't encouraging for the bull case, but they don't appear to be terribly dire either.

Let's now look at results if instead of entering after the 1st trigger, you purchase only if the trigger is at least the 2nd one in a 30-day period, which is a common time-period that Hindenburg watchers look for.

Buy SPX when the 2nd Hindenburg Omen triggers.
Sell X days later. \$100k/trade. 1980 - 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
100	26,898.95	13	8	5	61.54	8,036.45	17,883.98	-7,478.53	-18,879.12	1.07	1.72	2,069.15
95	23,070.79	14	9	5	64.29	7,381.26	17,605.78	-8,672.11	-21,212.88	0.85	1.53	1,647.91
90	22,054.63	14	10	4	71.43	6,172.13	20,476.59	-9,916.68	-20,011.68	0.62	1.56	1,575.33
85	7,163.52	15	7	8	46.67	9,200.25	20,455.19	-7,154.78	-21,883.68	1.29	1.13	477.57
80	6,472.48	15	8	7	53.33	7,696.39	18,961.47	-7,871.24	-21,961.68	0.98	1.12	431.50
75	10,263.99	15	8	7	53.33	7,890.59	17,861.51	-7,551.54	-23,181.60	1.04	1.19	684.27
70	-3,656.11	15	9	6	60.00	6,305.81	21,700.67	-10,068.06	-19,060.08	0.63	0.94	-243.74
65	-24,980.14	15	7	8	46.67	6,780.26	20,504.41	-9,055.25	-23,131.68	0.75	0.66	-1,665.34
60	-14,676.10	15	8	7	53.33	5,588.81	19,457.95	-8,483.79	-22,011.60	0.66	0.75	-978.41
55	-32,222.51	15	7	8	46.67	5,811.57	18,625.49	-9,112.94	-26,329.68	0.64	0.56	-2,148.17
50	-25,584.35	16	7	9	43.75	6,467.96	17,961.02	-7,873.34	-29,889.60	0.82	0.64	-1,599.02
45	-26,235.95	17	7	10	41.18	5,587.25	16,345.32	-6,534.67	-24,766.56	0.86	0.60	-1,543.29
40	-21,976.59	17	7	10	41.18	5,898.03	14,615.13	-6,326.28	-24,853.92	0.93	0.65	-1,292.74
35	-16,473.85	17	8	9	47.06	5,331.43	13,303.31	-6,569.47	-22,211.28	0.81	0.72	-969.05
30	-20,661.59	17	9	8	52.94	4,331.49	11,007.09	-7,455.63	-20,354.88	0.58	0.65	-1,215.39
25	-22,473.16	18	9	9	50.00	4,262.08	10,173.56	-6,759.10	-23,381.28	0.63	0.63	-1,248.51
20	-30,025.89	19	7	12	36.84	3,944.37	8,886.35	-4,803.04	-22,295.52	0.82	0.48	-1,580.31
15	-1,896.70	20	8	12	40.00	3,145.17	8,305.02	-2,254.84	-6,748.56	1.39	0.93	-94.84
10	-6,714.63	26	8	18	30.77	2,981.07	9,247.23	-1,697.96	-5,748.21	1.76	0.78	-258.26
5	-3,288.28	34	12	22	35.29	2,221.24	6,245.73	-1,361.05	-3,352.36	1.63	0.89	-96.71

Some of these numbers look a little worse, but you'd probably need to squint to notice. I next checked instances that triggered a 3rd signal in a 30-day period.

Buy SPX when the 3rd Hindenburg Omen triggers.
Sell X days later. \$100k/trade. 1980 - 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
100	24,547.43	10	7	3	70.00	6,497.67	18,512.90	-6,978.75	-16,085.07	0.93	2.17	2,454.74
95	14,171.68	10	6	4	60.00	6,404.26	16,070.66	-6,063.47	-16,770.54	1.06	1.58	1,417.17
90	1,060.35	10	5	5	50.00	7,421.31	18,595.58	-7,209.24	-19,277.67	1.03	1.03	106.03
85	9,240.07	10	6	4	60.00	7,078.03	18,884.96	-8,307.03	-21,362.25	0.85	1.28	924.01
80	-7,227.80	11	5	6	45.45	7,540.10	16,528.58	-7,488.05	-19,449.82	1.01	0.84	-657.07
75	997.16	11	5	6	45.45	9,641.47	18,289.24	-7,868.36	-22,758.23	1.23	1.02	90.65
70	-9,972.66	11	5	6	45.45	7,622.19	19,119.22	-8,013.93	-21,021.08	0.95	0.79	-906.61
65	-24,312.51	11	4	7	36.36	6,515.62	17,909.76	-7,196.43	-23,731.66	0.91	0.52	-2,210.23
60	-24,033.87	11	4	7	36.36	5,846.03	17,209.10	-7,903.00	-22,576.69	0.74	0.49	-2,184.90
55	-29,102.66	11	3	8	27.27	7,196.06	17,905.52	-6,336.35	-20,673.65	1.14	0.43	-2,645.70
50	-18,897.71	12	4	8	33.33	7,428.85	17,255.74	-6,076.64	-22,263.69	1.22	0.61	-1,574.81
45	-28,482.23	12	5	7	41.67	5,102.88	15,507.80	-7,713.81	-25,143.29	0.66	0.47	-2,373.52
40	-38,157.63	12	4	8	33.33	5,582.58	13,700.50	-7,560.99	-26,846.01	0.74	0.37	-3,179.80
35	-29,355.64	12	3	9	25.00	6,823.64	11,461.78	-5,536.29	-22,795.79	1.23	0.41	-2,446.30
30	-29,214.58	13	6	7	46.15	4,754.90	10,991.14	-8,249.14	-23,844.34	0.58	0.49	-2,247.28
25	-36,178.35	13	5	8	38.46	4,444.14	9,841.04	-7,299.88	-25,105.73	0.61	0.38	-2,782.95
20	-41,061.44	13	4	9	30.77	4,136.00	8,458.80	-6,400.61	-21,406.07	0.65	0.29	-3,158.57
15	-34,465.23	15	6	9	40.00	3,205.22	7,078.68	-5,966.28	-26,924.26	0.54	0.36	-2,297.68
10	-42,296.03	17	5	12	29.41	1,892.94	3,159.86	-4,313.39	-25,784.94	0.44	0.18	-2,488.00
5	-13,719.37	22	6	16	27.27	1,564.02	4,174.28	-1,443.97	-3,509.22	1.08	0.41	-623.61

Between 35 and 55 days out there appears to be some pretty poor returns on a small sample size.

With the 4th trigger occurring on Tuesday I also updated the stats when 4 signals occur.

Buy SPX when the 4th Hindenburg Omen triggers. Sell X days later. \$100k/trade. 1980 - 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
100	10,753.93	7	5	2	71.43	3,275.36	7,362.09	-2,811.44	-3,671.20	1.17	2.91	1,536.28
95	8,459.44	7	3	4	42.86	5,663.41	6,207.97	-2,132.70	-4,635.15	2.66	1.99	1,208.49
90	-3,036.53	7	2	5	28.57	4,199.09	4,666.20	-2,286.94	-6,882.20	1.84	0.73	-433.79
85	1,098.95	7	3	4	42.86	4,450.55	7,141.18	-3,063.18	-6,553.95	1.45	1.09	156.99
80	1,156.14	7	3	4	42.86	4,702.76	7,248.39	-3,238.04	-6,169.80	1.45	1.09	165.16
75	-6,739.43	8	3	5	37.50	5,784.06	8,515.03	-4,818.32	-9,034.35	1.20	0.72	-842.43
70	-11,409.38	8	4	4	50.00	2,475.77	3,749.51	-5,328.12	-9,322.50	0.46	0.46	-1,426.17
65	-24,740.37	8	2	6	25.00	787.95	1,445.70	-4,386.04	-10,467.60	0.18	0.06	-3,092.55
60	-26,640.33	8	3	5	37.50	513.94	949.65	-5,636.43	-11,602.80	0.09	0.05	-3,330.04
55	-25,996.67	8	2	6	25.00	948.91	1,201.20	-4,649.08	-8,851.04	0.20	0.07	-3,249.58
50	-20,458.02	9	3	6	33.33	2,689.94	3,934.12	-4,754.64	-9,493.04	0.57	0.28	-2,273.11
45	-24,937.30	9	2	7	22.22	2,367.91	3,631.33	-4,239.02	-14,483.52	0.56	0.16	-2,770.81
40	-26,280.87	9	2	7	22.22	2,385.07	3,315.35	-4,435.86	-11,889.84	0.54	0.15	-2,920.10
35	-35,747.35	9	1	8	11.11	3,328.16	3,328.16	-4,884.44	-14,149.68	0.68	0.09	-3,971.93
30	-17,212.09	10	4	6	40.00	2,889.95	5,262.60	-4,795.31	-13,738.80	0.60	0.40	-1,721.21
25	-18,478.32	10	4	6	40.00	2,791.46	6,253.80	-4,940.70	-12,343.52	0.56	0.38	-1,847.83
20	-29,190.14	10	1	9	10.00	4,796.40	4,796.40	-3,776.28	-9,672.80	1.27	0.14	-2,919.01
15	-22,060.04	10	2	8	20.00	3,896.04	4,301.89	-3,731.52	-8,414.48	1.04	0.26	-2,206.00
10	-18,522.59	14	4	10	28.57	1,570.31	2,279.81	-2,480.38	-6,566.95	0.63	0.25	-1,323.04
5	-15,562.01	15	3	12	20.00	1,274.64	2,769.90	-1,615.49	-4,884.75	0.79	0.20	-1,037.47

There are only 9 instances when looking out 35-45 days, but with 8 of them being down 35 days later these results warrant closer investigation. Below are the individual instances.

Buy SPX when the 4th Hindenburg Omen triggers. Sell 35 days later. \$100k/trade. 1980 - present.				
Date/Time	Signal	Price	% Profit	Run-up Drawdown
02/14/80	Buy	\$116.72	(14.16%)	\$1,001.52
04/07/80	Sell	\$100.19		(\$16,264.00)
07/24/86	Buy	\$237.94	(3.06%)	\$6,846.00
09/12/86	Sell	\$230.66		(\$3,864.00)
03/15/94	Buy	\$467.01	(3.35%)	\$873.12
05/05/94	Sell	\$451.38		(\$6,666.10)
12/08/99	Buy	\$1,403.88	(3.11%)	\$5,262.52
01/28/00	Sell	\$1,360.16		(\$3,385.28)
04/24/06	Buy	\$1,308.11	(6.45%)	\$1,412.84
06/13/06	Sell	\$1,223.69		(\$6,504.84)
07/20/07	Buy	\$1,534.10	(5.37%)	\$853.45
09/10/07	Sell	\$1,451.70		(\$10,627.50)
10/25/07	Buy	\$1,514.39	(3.07%)	\$2,532.42
12/14/07	Sell	\$1,467.95		(\$7,147.14)
06/04/13	Buy	\$1,631.38	3.34%	\$4,111.40
07/24/13	Sell	\$1,685.94		(\$4,334.05)
08/09/13	Buy	\$1,691.42	(0.58%)	\$2,267.96
09/30/13	Sell	\$1,681.55		(\$3,773.05)

The June instance did not conform, and saw a 3.3% gain 35 days later. But it DID post a drop of 4.3% during this period before staging that rebound. So the numbers still appear to favor the bears. And it is impressive that all 9 instances dipped at least 3% below the close of the 4th Hindenburg day at some point in the next 35 days. And the avg drawdown is about 2.5x the avg run-up.

In all, there just is not enough data for me to make a strong statement about the Hindenburg Omen. But when there have been 3-4 signals in the past, market difficulty has commonly occurred. My take is that the 4-cluster Hindenburg Omen we are now seeing is a possible warning sign. I think results are strong enough to give it some consideration and I have again included it on the intermediate-term active list.

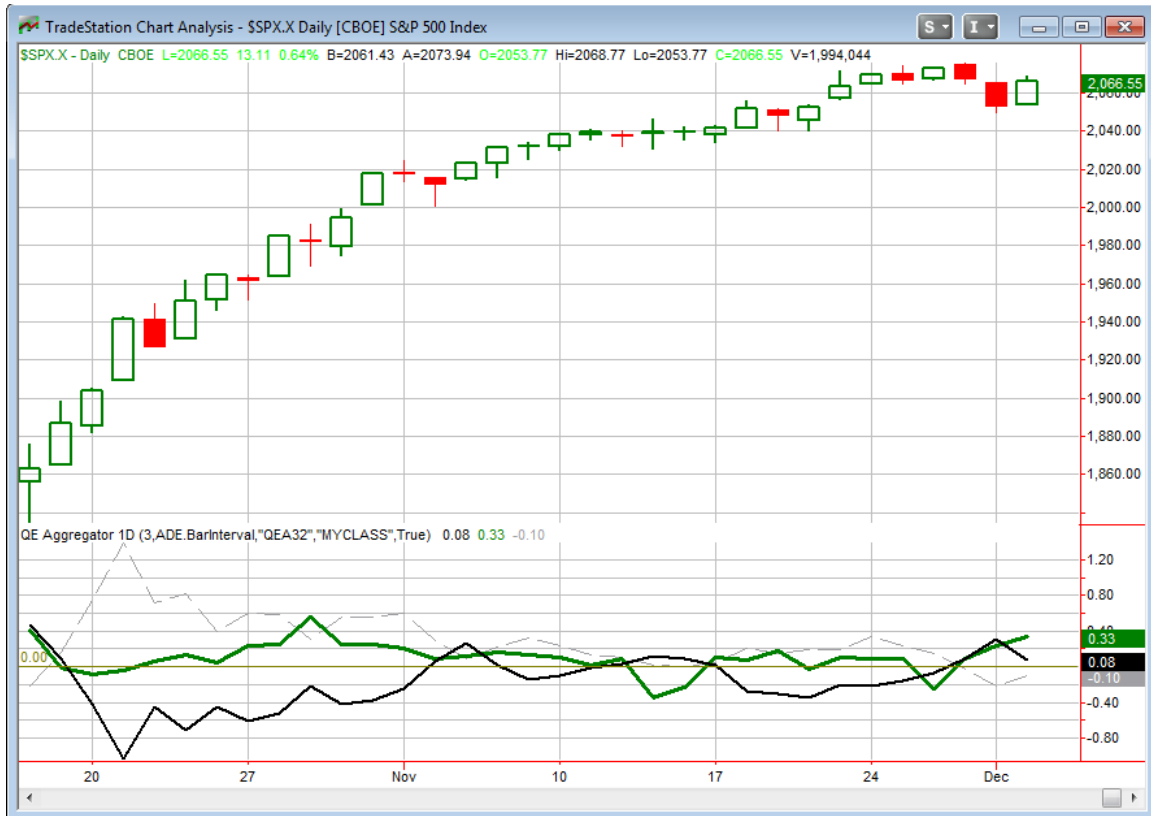
Subscribers that wish to study Hindenburgs more on their own may download the Tradestation strategy code from the member downloads section.

<http://quantifiableedges.com/other-code-spreadsheets/>

I would also note that Tom McClellan wrote an interesting piece on the history of the indicator a while back. You may find a link to that write-up below.

http://www.mcoscillator.com/learning_center/kb/special_market_reports/hindenburg_om_en_signaled_but_also_not/

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



Tonight the green Aggregator Line stayed well above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile, the black Differential Line held barely above 0. The positive Differential Line reading means the SPX is considered 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 below 0. Therefore the Aggregator signal stayed long at the close.

Expectations are set to remain bullish on Wednesday. Of course this could change if compelling bearish evidence emerges. The Differential Pivot will be *slightly inverted* at 2065.77 on Wednesday. This is less than 1 point *below* Tuesday's close. An inverted pivot means that the Differential Line will cross through 0 if SPX closes flat. In this case, SPX is going to need to close down about 1 point in order to remain "oversold"

versus expectations. Any flat or up close will turn SPX short-term overbought as measured by the Differential calculation.

As I mentioned, the unfilled gap up was disappointing, because I did not get a fill on the QE trade idea from last night. Hopefully most traders were able to take advantage of the pullback anyway. With the Differential Pivot now inverted, this is not an ideal entry point for me. Inverted pivots generally mean potential reward is limited to 1 day of gains. When I am in a trade I generally use inverted pivots as opportunities to begin scaling out – not in further. I believe the bounce still has further to go. The study from last night that looked at SPY closing below the 10 ma for the 1st time in over 25 days suggested a high likelihood that the uptrend would reassert itself and continue higher over the next several days and weeks. So while I believe there is plenty more upside to come, the market just does not seem set up for a great short-term entry right here.

Intermediate-term Outlook (2 weeks – 2 months) – updated 12/1 – somewhat bullish

The intermediate-term outlook was last updated in the 12/1/14 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.

None tonight

Current Open Trade Ideas

None

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