

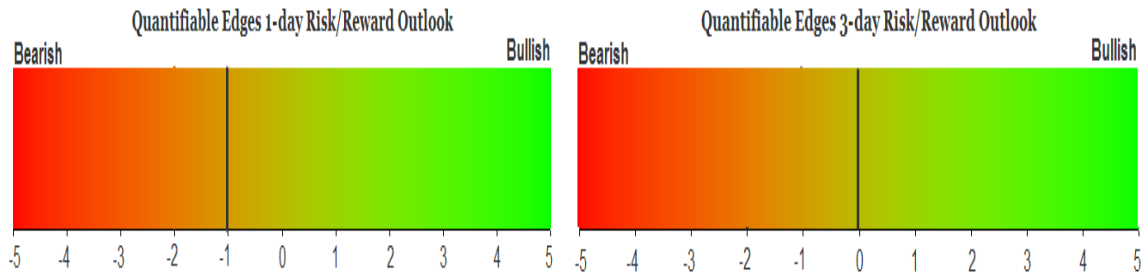
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 11, 2015

Volume 8 Issue 89

Market Overview



Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing
Flat	50% Long XIV	Flat

Tonight's Research Points

- Big VXO drops often spell trouble for the market the next day.

Short-term Outlook

The Bottom Line

Evidence tonight is pointing to a possible decline on Monday, but it only appears to be a 1-day inclination. With overall evidence mixed/slightly bullish and the market overbought I am neutral.

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						
May 11, 2015	VXO declines 20% in 1 day	1 day	Bearish			
May 6, 2015	1% drop on 2:1 negative breadth > 200	1-9 days	Bullish	3.00%	-2.50%	-5.40%
April 28, 2015	20-high poor close	1-10 days	Bullish	2.10%	-1.35%	-2.70%
Active - Long Term						
May 1, 2015	2 unfilled gaps down > 200. 5-day low	1-10 days	Bullish	2.50%	-1.70%	-3.40%
November 3, 2014	Quantitative Easing Ends	int term	Bearish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			
February 1, 2012	Golden Cross	int term	Bullish			
Dropped Tonight						
May 1, 2015	2 unfilled gaps down > 200. 5-day low	1-6 days	Bullish	1.90%	-1.30%	-2.40%

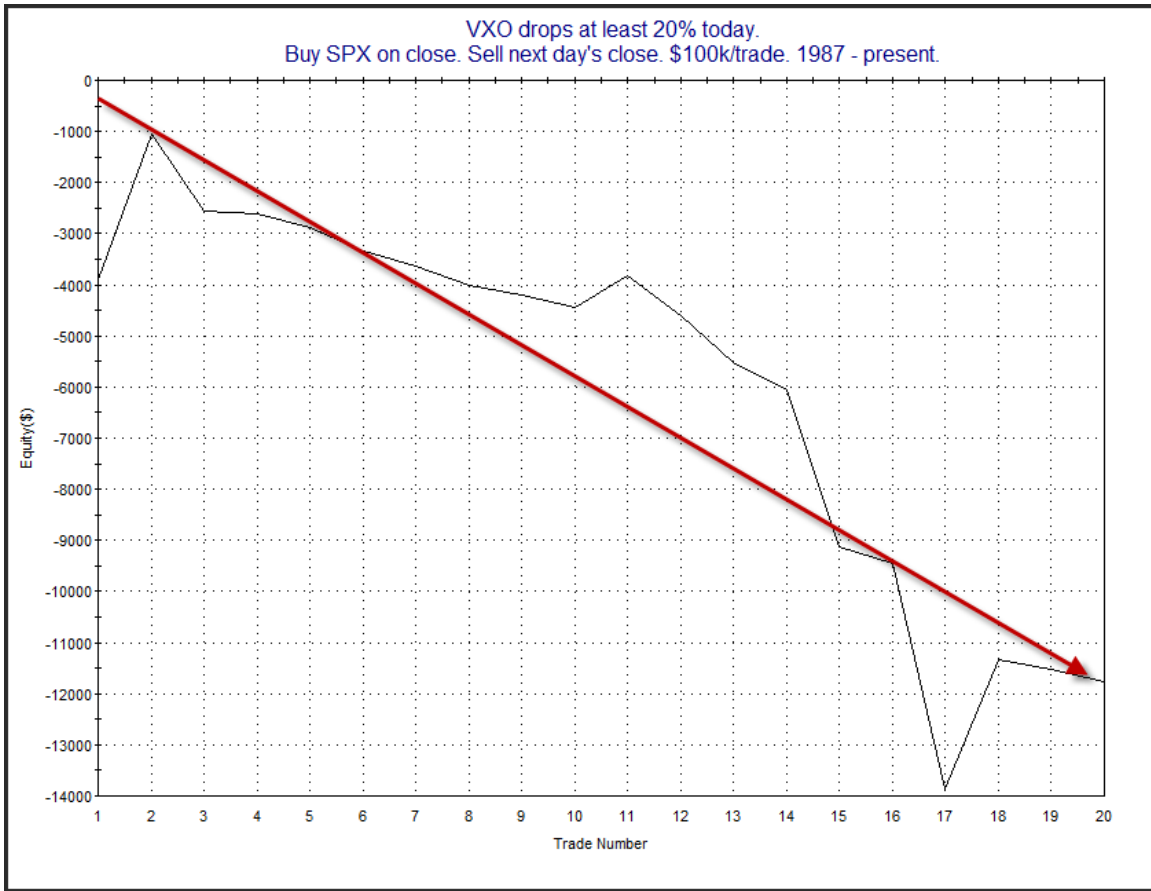
The Evidence

A positive reaction to the Employment Report kicked off a strong day on Friday. The SPX rose 1.35%, the NASDAQ rallied 1.2%, and the Russell 2000 gained 0.8%. Breadth was strongly positive as the NYSE Up Issues % came in at 80% and the Up Volume % was 84%. Total NYSE volume declined from the level of the last few days.

The VIX, which is a measure of options pricing and is often referred to as a “fear index” saw a 15% drop on Friday. Meanwhile, the VXO, which is the old measure of the VIX declined nearly 22%. Such big declines often suggest short-term over-optimism on the part of traders and are followed by a dip the next day. This can be seen in the study below, which was from the 1/2/13 letter. All stats are updated.

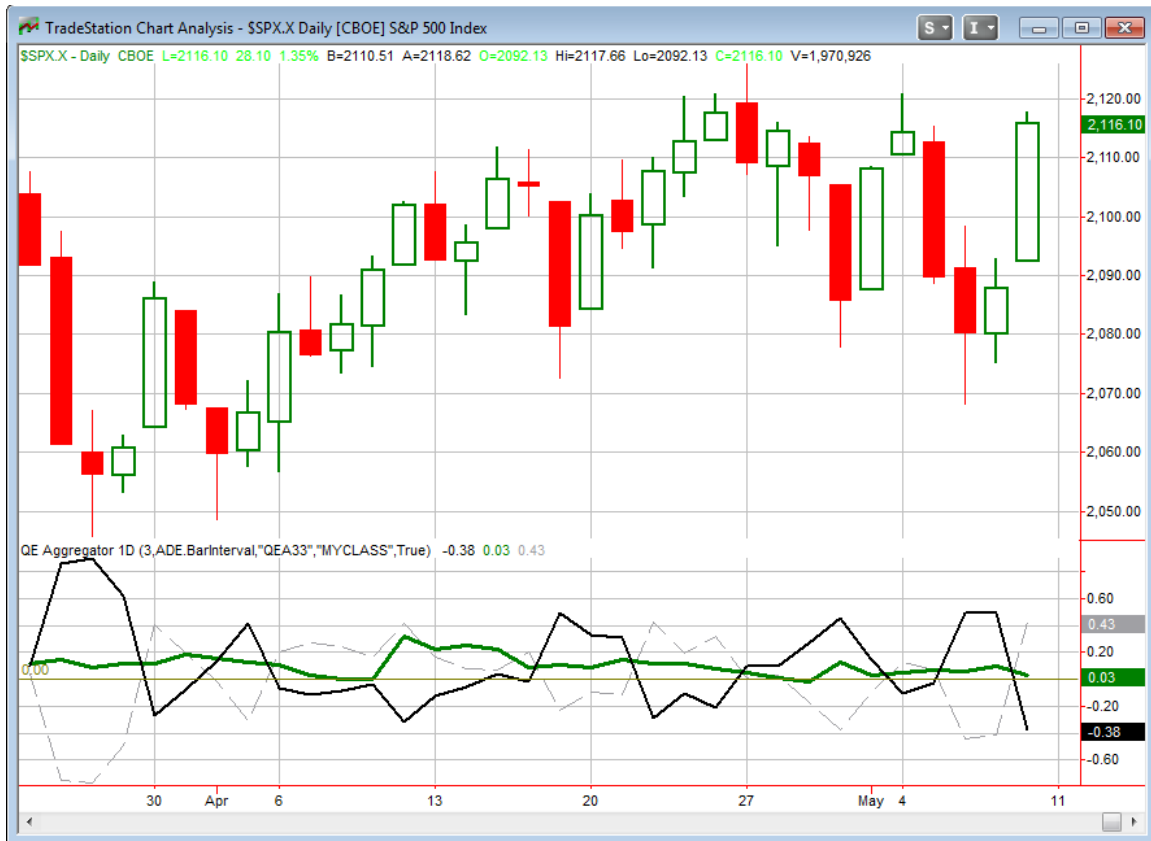
TradeStation Performance Summary Collapse ^			
All Trades			
Total Net Profit	(\$11,761.33)	Profit Factor	0.34
Gross Profit	\$5,997.43	Gross Loss	(\$17,758.76)
Total Number of Trades	20	Percent Profitable	15.00%
Winning Trades	3	Losing Trades	17
Even Trades	0		
Avg. Trade Net Profit	(\$588.07)	Ratio Avg. Win:Avg. Loss	1.91
Avg. Winning Trade	\$1,999.14	Avg. Losing Trade	(\$1,044.63)
Largest Winning Trade	\$2,860.08	Largest Losing Trade	(\$4,400.45)

Numbers here suggest a downside edge. Below is a profit curve to see how it has played out over time.



A bit choppy but it certainly appears the big VXO drops don't often bode well for the next day. This study has been added to the Short-Term Active List.

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



Even with tonight's bearish study the green Aggregator Line held a little above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile, the black Differential Line dove down below 0. The negative Differential Line reading means the SPX is overbought versus recent expectations. So expectations are positive but the SPX is overbought. This is considered a neutral configuration. Neutral configurations are visible on the chart whenever both lines close on opposite sides of 0. Therefore the Aggregator signal turned flat at the close.

Based on the current active studies, expectations are set to remain bullish on Monday. This could change if compelling bearish evidence emerges. The Differential Pivot will be 2083.34 on Monday. That is 1.5% below Friday's close. So SPX would need to close down at least this much in order to be considered "oversold" versus expectations. That would be a very large 1-day decline. A more likely scenario for working off the overbought condition would be a multi-day decline or consolidation.

While 3-day expectations are positive, the 1-day expectations are negative. Nimble traders could try and take advantage of a Monday decline. I don't try and trade that nimble and prefer to look for multi-day moves to profit. So I will not be looking to take on any new exposure on Monday, but will wait for the next favorable risk/reward opportunity to emerge.

Intermediate-term Outlook (2 weeks – 2 months) – updated 5/4– neutral

Combo #1	Combo #2	Combo #3
Long	Long	Flat

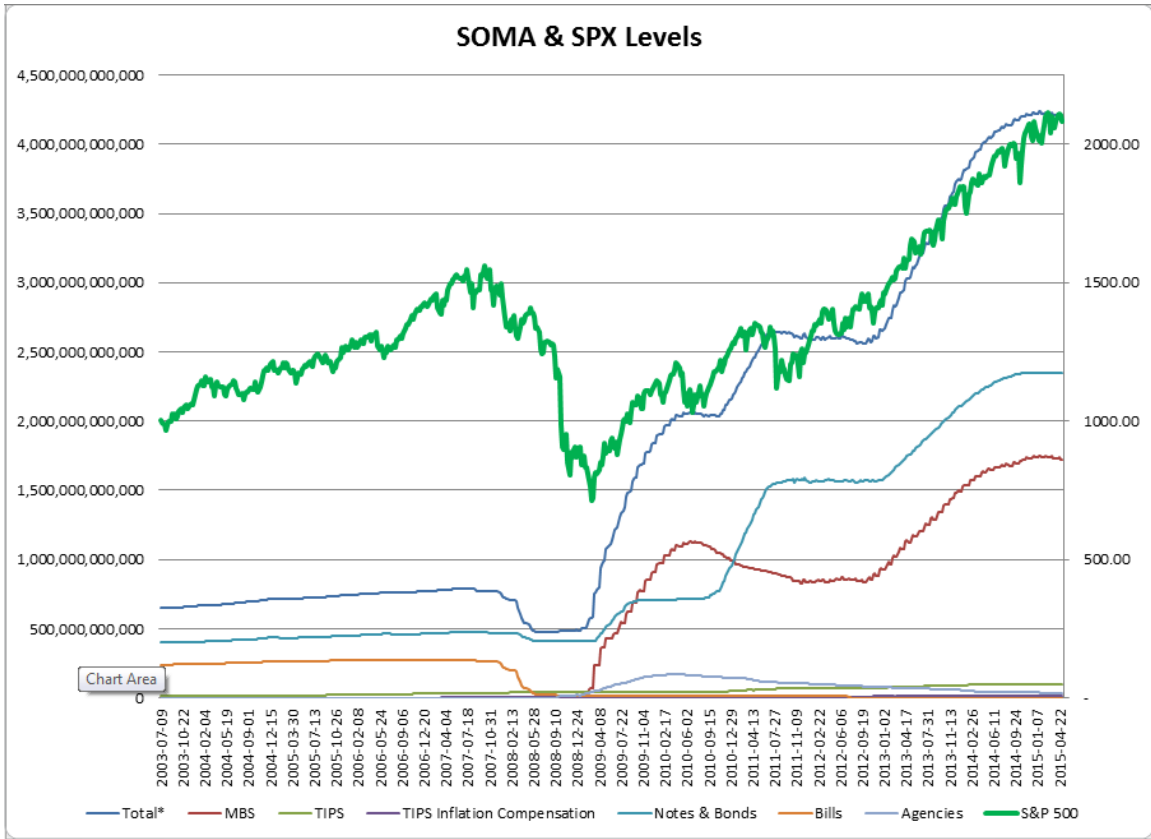
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#), which is included with all annual subscriptions. Detailed descriptions of these combination approaches can be found in [Lesson 8](#). Subscribers may also download detailed hypothetical historical performance reports covering 12/31/71 – 3/7/14 in [Lesson 11, Course Downloads](#). (You must go through the course first in order to access the Downloads.)

The major indices were split this week. The NASDAQ declined about 2 points, but the rally on Friday allowed the SPX to eek out a 0.4% gain. At this point there is not any strong indication that the uptrend is over.

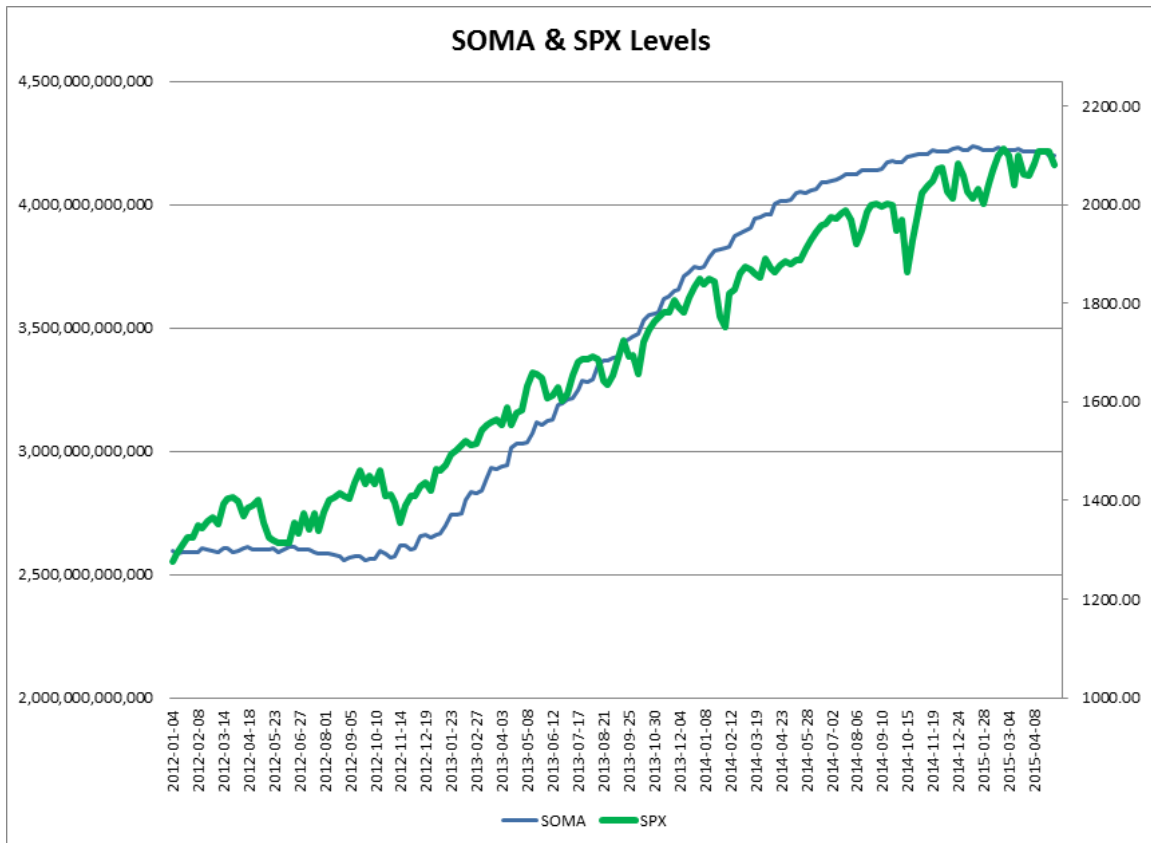
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

SOMA stands for System Open Market Account. It is the account at the Fed that contains all of its bond purchase holdings. We have tracked Fed purchases for several years, and as is evident in the charts below, the stock market has consistently reacted positively when the Fed has been buying securities in the open market and increasing the size of its account. When the account has declined, the market has struggled. The obvious takeaway has been “don’t fight the Fed”. As far as intermediate-term indicators go, this has been as good as anything in recent years.

While the Fed is not making new QE purchases any longer, it is continuing to reinvest maturities. Therefore, the total assets in their System Open Market Account (SOMA) has not begun to dive like the old Quantifiable Edges POMO indicators did. Below are long and short-term views of SOMA and SPX. First, the long-term view (back to 2003).



And now the zoomed-in view (2012 – present).



After a big decline the previous week, the SOMA level came in close to breakeven, with just a very small increase this past week. It is too soon to tell whether the tide has changed and the SOMA account will continue to shrink. But a shrinking SOMA would put pressure on the market and make a continuation of the bullish trend more difficult. Fed policy changes and SOMA activity remain an important market influence. I will continue watching SOMA levels closely.

Not only did SOMA barely budge and the market finish split/near flat for the week, but there was nothing else from an intermediate-term perspective that seemed to provide a strong hint. Indications from last week remain in force.

The trend still appears to be upwards, and we do still have a price-action based intermediate-term study suggesting more upside. But other indicators continue to suggest a dangerous environment. This includes the diverging number of stocks making new highs, the fact that the market is now in the “Worst 6 Months”, the questionable SOMA action, and the lagging NASDAQ. A stable or rising SOMA, or a flip in the NASDAQ/SPX Relative Strength Indicator could still improve the outlook. For now I remain neutral. From a trading standpoint that means I will be willing to consider both long and short positions, but I will probably be taking conservative entries with both.

Catapult and Capitulative Breadth Statistics

[Catapult & CBI Presentation Link](#)

Open Catapult Triggers

HAL @ \$46.35 (bought 1/3 @ limit)

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 1(HAL)

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

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
XIV(1/2)	3/9/2015	\$32.25	\$41.98	30.17%	\$37.90	Aggressive VIX
SPY (1/4)	5/6/2015	\$208.04	\$211.62	1.72%		<i>sold on close</i>
HAL(1/3)	5/8/2015	\$46.35	\$48.11	3.80%		Catapult

SPY was sold at the close as I indicated in the last letter.

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