

QUANTIFIABLE EDGES

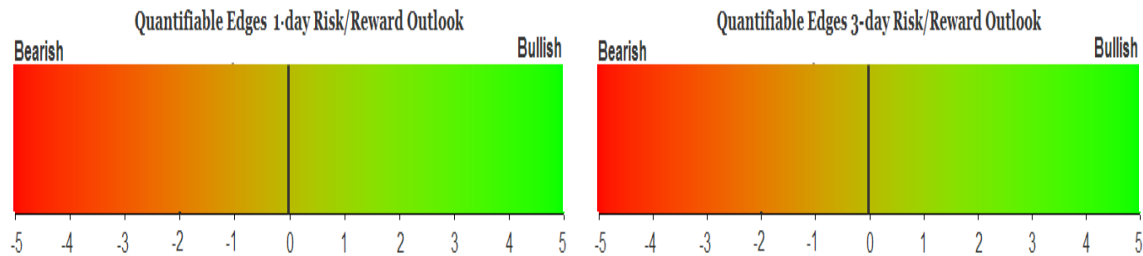
WEEKLY RESEARCH

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 31, 2016

Issue 367

Market Overview



Signals Overview

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

Tonight's Research Points

- Friday's seemingly low volume was actually normal for the Friday before Memorial Day.
- The week of Memorial Day was strong for a long time, but it has had a tough time the last few years – except for Thursday.
- SPY hitting the first closing high in a while along with an unfilled gap up sets up a bullish scenario.
- The NASDAQ has moved into a leading position – a bullish intermediate-term indication.

Short-term Outlook

The Bottom Line

Evidence has turned slightly bullish but the market is a little short-term overbought. This leaves me neutral.

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

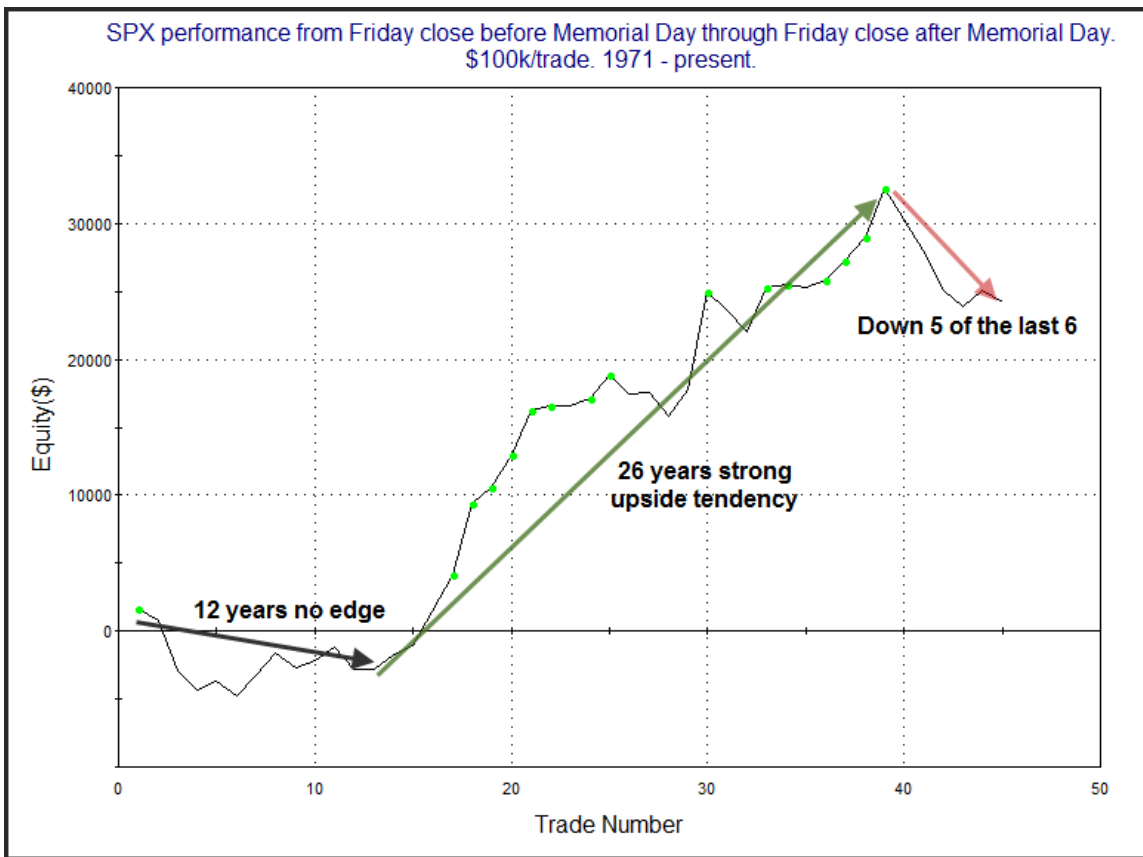
Study Date	Description	Time span	Bias	Avg Run-up	Avg DrawDn	Avg DrawDn - 1 Std Dev
Active - Short Term						
May 31, 2016	SPY breakaway gap	1-5 days	Bullish	1.50%	-1.00%	-2.00%
May 27, 2016	Down today. RSI2 > 90/	1-2 days	Bullish			
May 25, 2016	QE Buying Power Short Signal	1-6 days	Bearish			
Active - Long Term						
May 31, 2016	NASDAQ Leading	int term	Bullish			
May 24, 2016	Bounce from 20-low then inside day dn.	1-10 days	Bullish	5.00%	-2.85%	-6.75%
May 17, 2016	20-low to 4-high	1-20 days	Bullish	3.80%	-2.10%	-4.55%
April 26, 2016	Golden Cross	int term	Bullish			
March 2, 2016	FTD & 20-day high	int term	Bullish			
February 18, 2016	Up Issue % > 70% 3x	1-85 days	Bullish	10.70%	-5.10%	-12.10%
February 1, 2016	2 90% up days in 1 week	1-9 months	Bullish	23.10%	-6.60%	-15.10%
November 3, 2014	Quantitative Easing Ends	int term	Bearish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			
Dropped Tonight						
May 9, 2016	CBI >= 7. SPX < 200.	1-15 days	Bullish			

The Evidence

Friday saw the market post further gains. The SPX rose 0.4%, the NASDAQ gained 0.7%, and the Russell 2000 rallied 0.9%. Breadth was positive as the NYSE Up Issues % was 64% and the Up Volume % came in at 63%. NYSE volume came in at the lightest level in a while.

There were several studies that appeared in the Quantifinder that keyed off the extremely low volume. I am not inclined to dwell on any of them. Extremely low volume on a “normal” day can be a useful bit of information. On the day before Memorial Day weekend, extremely low volume is normal. Looking back to 1998, there have only been 2 years when NYSE volume did NOT come in at the lowest level in 20 days. Those were 2008 and 2010. Other than that, every year has seen extremely low volume. Memorial Day did bring up some other studies, though.

The week of Memorial Day has shown some interesting seasonal tendencies over the years. But it has faltered greatly the last few. The chart below is from the 5/26/15 subscriber letter and has been updated. It examines SPX performance from the Friday before Memorial Day to the Friday after it.

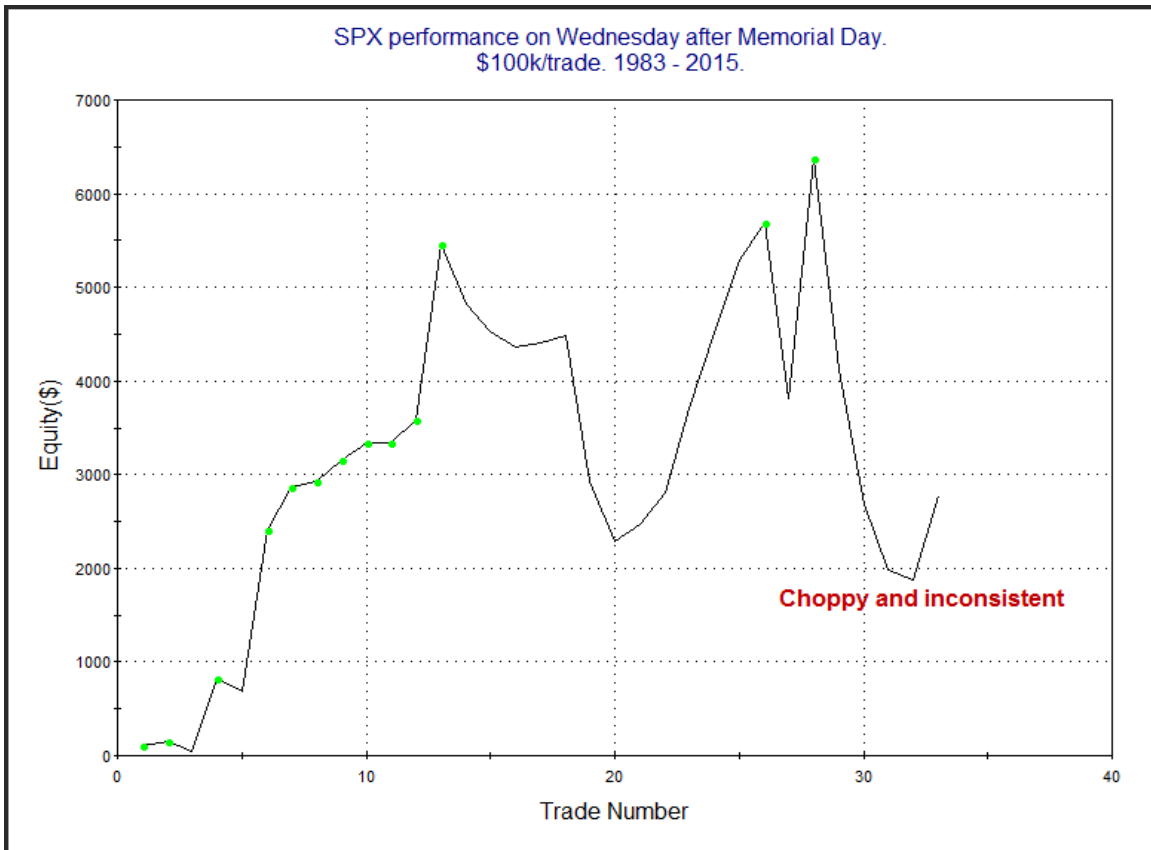
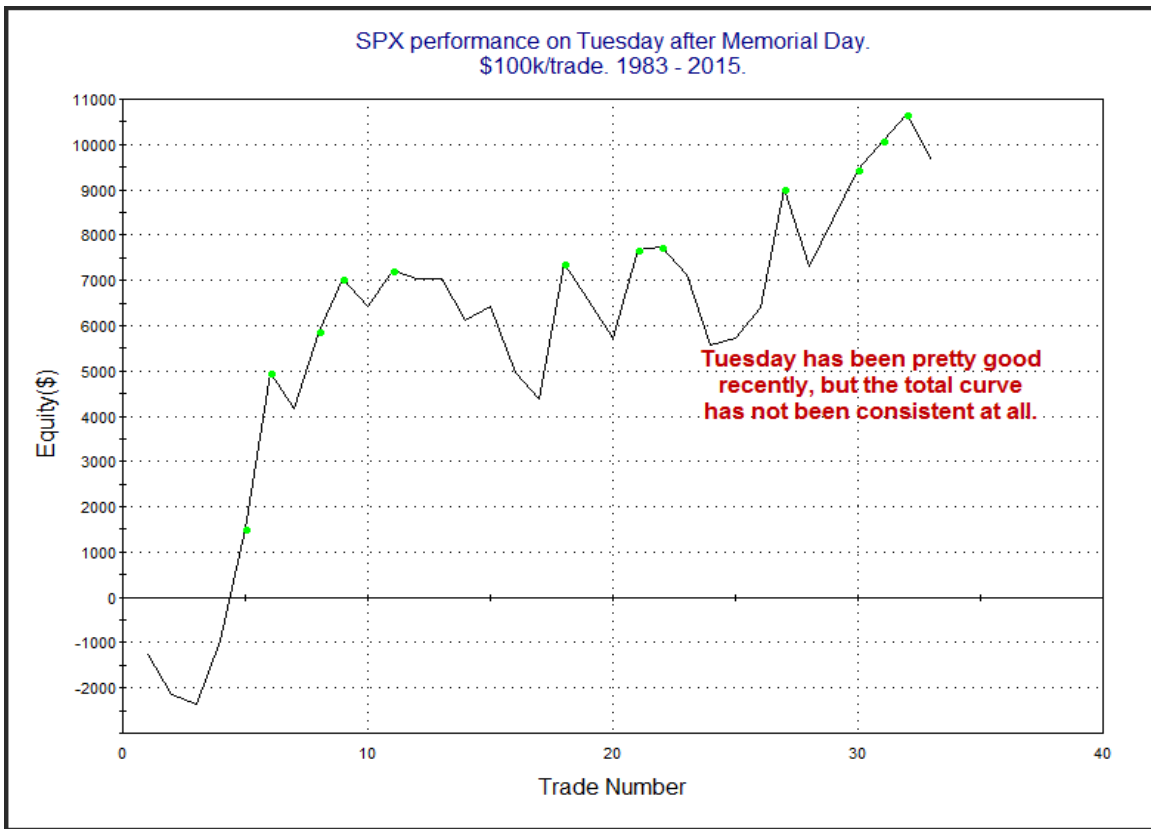


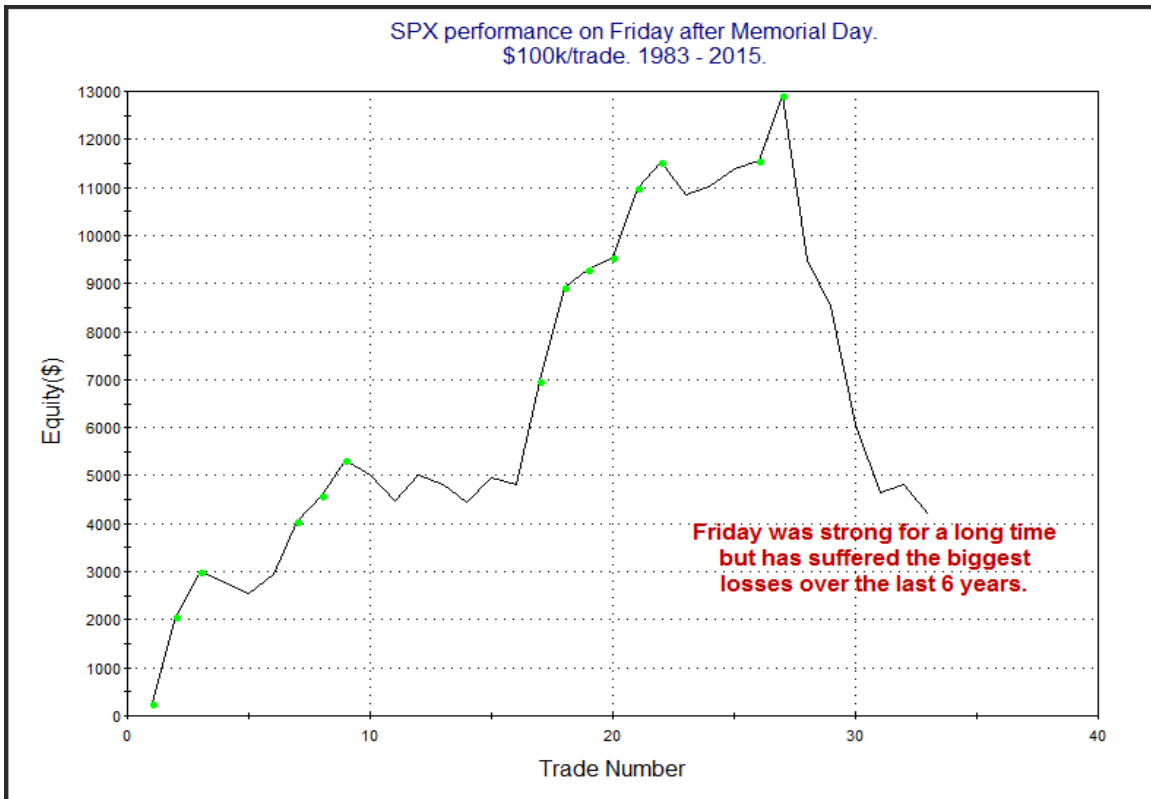
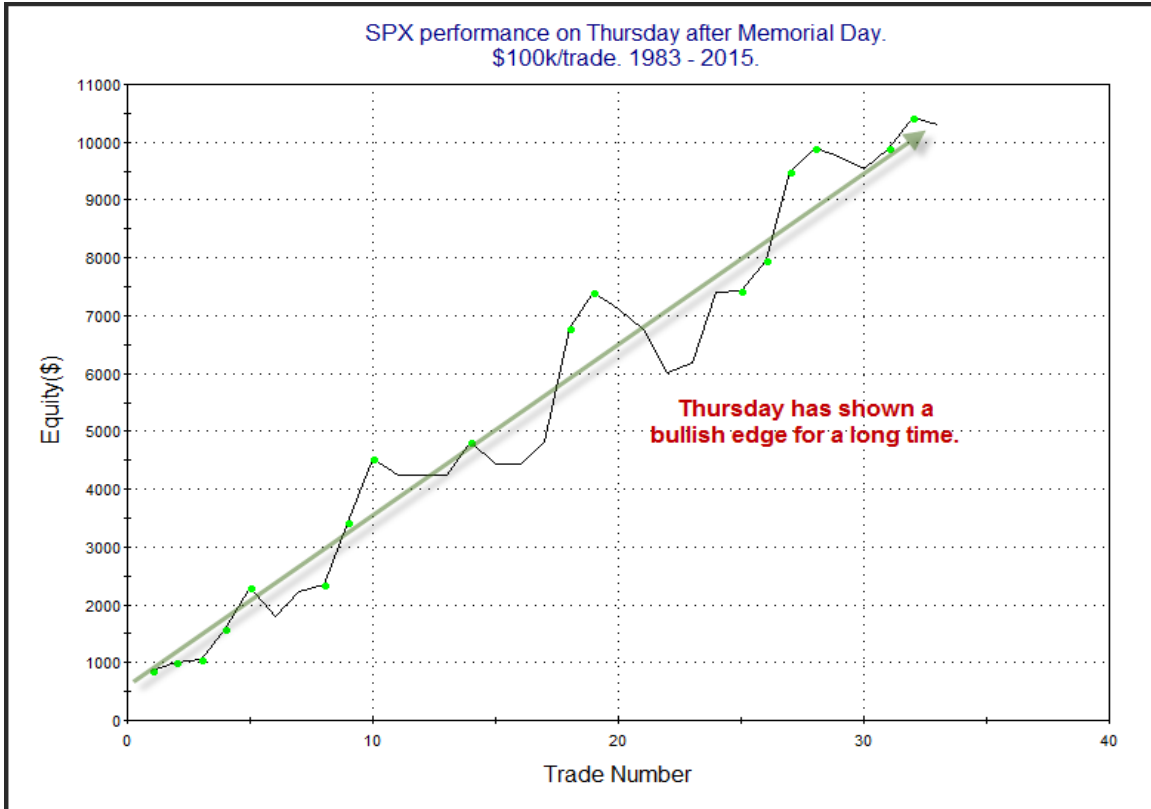
There was no substantial edge apparent throughout the 70s, but starting in 1983 through 2009 there was a bullish tendency. The last 6 years this week has mostly struggled. Last year I took a day by day look. I decided to do that again to see where the market has struggled recently. Returns are broken down by the day of the week.

SPX performance on X Day of Memorial Week.
\$100k/trade. 1983 - 2015.

Day of Week	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
Fri	4,195.26	33	20	13	60.61	790.02	2,140.16	-892.71	-3,415.50	0.88	1.36	127.13
Thurs	10,306.72	33	23	9	69.70	580.14	1,970.50	-337.39	-735.68	1.72	4.39	312.32
Wed	2,774.38	33	21	12	63.64	604.23	2,573.31	-826.21	-2,268.10	0.73	1.28	84.07
Tues	9,645.46	33	17	16	51.52	1,361.16	3,443.56	-843.40	-1,701.70	1.61	1.71	292.29

The results table suggests Thursday is the most consistently bullish day. Wednesday has the weakest net numbers. So let's examine the equity curves for each particular day.





The charts seem to confirm what the results table was suggesting. Thursday appears to be the only day that I'm inclined to credit a consistent seasonal edge to at this point.

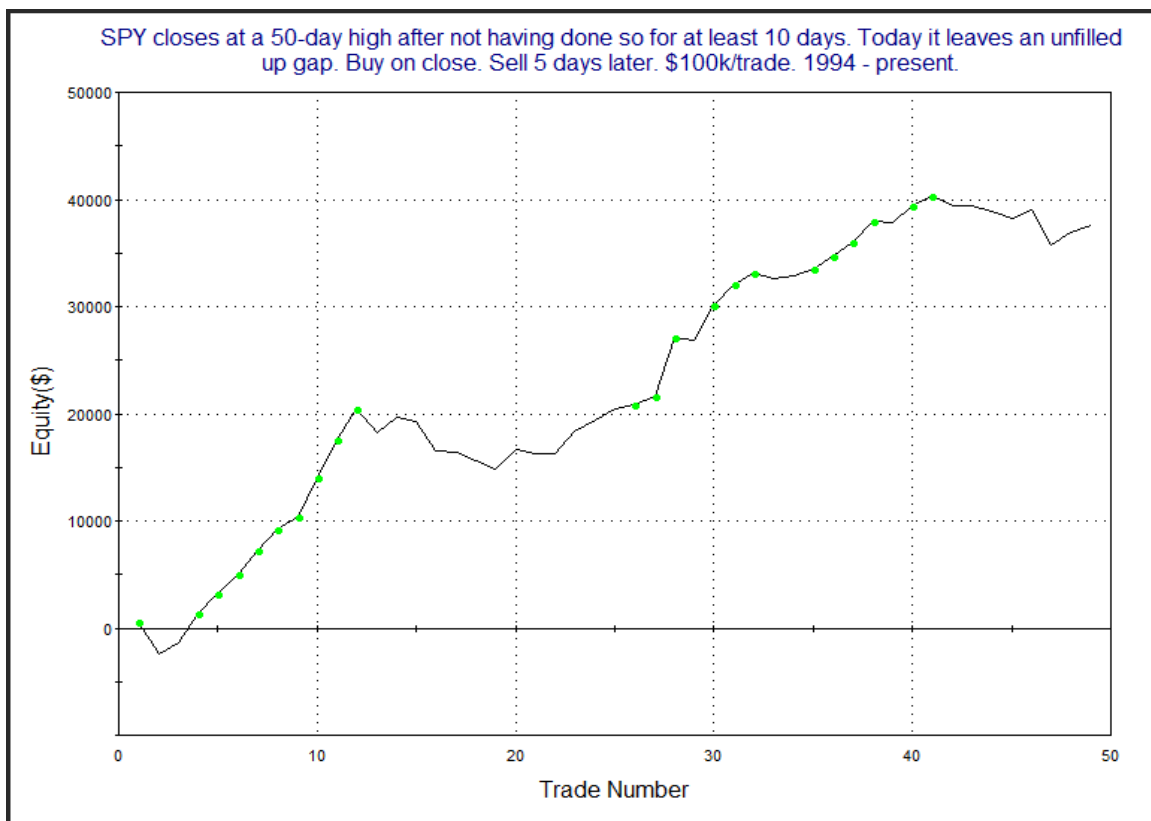
It is also notable that SPY left an unfilled gap up on Friday. And it closed at the first 50-day high in a while (though SPX just missed). In the 5/13/15 subscriber letter I looked at the importance of an unfilled upside gap on new high breakouts for SPY. I have revisited that study below.

SPY closes at a 50-day high after not having done so for at least 10 days. Today it leaves an unfilled up gap. Buy on close. Sell X days later. \$100k/trade. 1994 - 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	37,518.46	49	34	15	69.39	1,591.96	5,434.00	-1,107.21	-3,218.88	1.44	3.26	765.68
4	25,129.06	49	34	15	69.39	1,209.85	3,637.92	-1,067.06	-3,267.84	1.13	2.57	512.84
3	19,667.95	49	33	16	67.35	1,067.73	3,992.56	-972.95	-2,538.18	1.10	2.26	401.39
2	15,888.68	49	33	16	67.35	787.26	2,545.92	-630.69	-2,293.20	1.25	2.57	324.26
1	6,709.13	49	36	13	73.47	474.81	1,816.10	-798.77	-2,591.68	0.59	1.65	136.92

45 of 49 instances (92%) closed above the entry price at some point in the next week.

Results here are strong across the board. Below is an equity curve using a 5-day holding period.



The curve has struggled a bit recently, but I still believe it is strong enough to give this study some consideration.

Technicians will often use the term “breakaway gap”. This suggests the gap occurs on the same day as a base breakout. The idea is that the new high causes excitement and the gap leaves a good amount of people sidelined or stuck short. When it doesn’t immediately fill, it leads these people to chase and helps to propel the market even higher.

Now let’s look at instances where the 50-day high breakout was not accompanied by an unfilled gap. Interestingly, the number of instances was very close. This study also appeared in the 5/13/15 letter and has been updated.

SPY closes at a 50-day high after not having done so for at least 10 days. Today it does NOT leave an unfilled up gap. Buy on close. Sell X days later. \$100k/trade. 1994 - 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	2,339.30	42	25	17	59.52	1,009.69	2,671.20	-1,347.23	-4,285.26	0.75	1.10	55.70
4	-1,337.93	42	23	19	54.76	1,027.10	2,072.07	-1,313.75	-4,518.34	0.78	0.95	-31.86
3	3,501.94	42	24	18	57.14	1,045.18	2,927.90	-1,199.03	-5,133.72	0.87	1.16	83.38
2	-2,142.36	42	21	21	50.00	663.67	2,324.90	-765.68	-3,640.86	0.87	0.87	-51.01
1	2,173.24	42	23	18	54.76	483.02	1,586.97	-496.46	-2,448.72	0.97	1.24	51.74

Moves to new highs that don't start with an unfilled gap are much less reliable.

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



With tonight's evidence included the green Aggregator Line inched back above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line held below 0. The negative Differential Line reading means SPX is overbought versus recent expectations. So expectations are positive but 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.

With the current list of active studies, expectations are poised to remain positive on Tuesday. Of course this could change if new bearish evidence emerges. The Differential Pivot will be 2096.71 on Tuesday. That is just 0.1% below Friday's close. So it will only take a mild down close for SPX to move from overbought to oversold versus recent expectations on Tuesday.

The Aggregator is neutral and so am I. Long-side evidence is leading here but I would prefer to see a bit of a pullback to buy into. If we get a pullback early in the week I could very well be looking to get long Wednesday or Thursday. For now I will remain mostly sidelined and patient.

Intermediate-term Outlook (2 weeks – 2 months) – updated 5/31 – bullish

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

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.) *This week Combo #3 changed to “Long” to match up with the other 2 Combo Systems.*

This was a strong rally week from the market, with the SPX gaining 2.3% and finishing just below its April closing high. We saw an interesting study trigger on Monday with intermediate-term implications. Below I have copied some of that research from Monday night's letter.

Action today was a continuation of the recent chop. Monday marked the 6th day in a row that SPX reversed direction on a closing basis. Friday's bounce off a 20-day low on Thursday did not get any follow through today. But bulls should not be too discouraged by this. The study below last appeared in the 8/11/11 subscriber letter. It considers similar situations in the past. I have updated all the stats.

SPY either closes at a 20-day low 2 days ago or makes a 20-day intraday low yesterday.
 Yesterday it closed up. Today is an inside day with a down close.
 Buy on close. Sell X days later. \$100k/trade. 1993 - 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	55,711.01	15	15	0	100.00	3,714.07	20,713.48	0.00	0.00	100.00	100.00	3,714.07
9	40,126.92	15	12	3	80.00	3,658.92	12,624.80	-1,260.02	-2,882.00	2.90	11.62	2,675.13
8	29,020.78	15	12	3	80.00	3,142.64	15,898.44	-2,896.97	-5,475.84	1.08	4.34	1,934.72
7	21,785.84	15	10	5	66.67	3,734.88	17,351.76	-3,112.60	-7,242.24	1.20	2.40	1,452.39
6	17,209.09	15	10	5	66.67	3,301.69	14,782.76	-3,161.55	-6,447.36	1.04	2.09	1,147.27
5	6,822.46	15	9	6	60.00	3,704.74	11,377.00	-4,420.03	-11,713.44	0.84	1.26	454.83
4	20,274.14	15	10	5	66.67	3,935.74	11,714.64	-3,816.66	-9,229.44	1.03	2.06	1,351.61
3	19,086.27	15	11	4	73.33	3,084.86	10,848.52	-3,711.79	-6,458.40	0.83	2.29	1,272.42
2	12,354.35	15	11	4	73.33	2,076.91	6,650.04	-2,622.92	-3,047.04	0.79	2.18	823.62
1	6,482.90	15	9	5	60.00	1,483.64	5,960.08	-1,373.98	-1,883.84	1.08	1.94	432.19

The stats certainly appear bullish and the edge seems to occur both right off the bat and after a couple of weeks. In the tables below I show dates and stats for ...(the) 10-day holding period.

SPY either closes at a 20-day low 2 days ago or makes a 20-day intraday low yesterday.
 Yesterday it closed up. Today is an inside day with a down close.
 Buy on close. Sell 10 days later. \$100k/trade. 1993 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
3/3/1994	Buy	\$46.56	1.48%	\$1,631.72
3/17/1994	Sell	\$47.25		(\$300.58)
5/9/2002	Buy	\$107.75	2.18%	\$3,248.00
5/23/2002	Sell	\$110.10		(\$1,995.20)
7/16/2002	Buy	\$90.56	0.42%	\$3,024.96
7/30/2002	Sell	\$90.94		(\$14,219.52)
10/2/2002	Buy	\$83.15	4.09%	\$6,695.14
10/16/2002	Sell	\$86.55		(\$7,308.16)
12/17/2002	Buy	\$90.85	0.24%	\$495.00
1/2/2003	Sell	\$91.07		(\$4,114.00)
8/30/2005	Buy	\$121.05	1.78%	\$3,047.94
9/14/2005	Sell	\$123.21		(\$256.06)
1/22/2009	Buy	\$82.75	2.20%	\$6,281.60
2/5/2009	Sell	\$84.57		(\$2,633.44)
3/9/2009	Buy	\$68.11	20.72%	\$20,816.24
3/23/2009	Sell	\$82.22		\$0.00
5/28/2010	Buy	\$109.37	0.13%	\$1,599.50
6/14/2010	Sell	\$109.51		(\$4,314.08)
8/30/2010	Buy	\$105.31	6.97%	\$7,573.02
9/14/2010	Sell	\$112.65		(\$778.18)
6/17/2011	Buy	\$127.05	5.41%	\$5,548.35
7/1/2011	Sell	\$133.92		(\$676.82)
8/10/2011	Buy	\$112.29	5.16%	\$7,929.90
8/24/2011	Sell	\$118.08		\$0.00
12/19/2013	Buy	\$181.49	0.48%	\$1,760.00
1/6/2014	Sell	\$182.36		(\$506.00)
10/9/2014	Buy	\$192.74	1.14%	\$1,792.28
10/23/2014	Sell	\$194.93		(\$5,604.76)
7/8/2015	Buy	\$204.53	3.34%	\$4,221.20
7/22/2015	Sell	\$211.37		\$0.00

I don't see any red flags here. This certainly appears to suggest an upside edge. I have included it on both the short and intermediate-term active lists.

The NASDAQ had an even stronger week than the SPX, rising 3.4%. The relative outperformance of the NASDAQ helped it to retake a leading position based on our NASDAQ/SPX Relative Strength Indicator. This is the first time the indicator has been positive since mid-April. Below is a chart of the indicator from the website.

NASDAQ/S&P 500 Relative Strength Weekly



The movement of the red line (which is about to turn green) above the blue line is our indication that the NASDAQ is in a leading position. Since 1971, nearly all of the S&P 500 gains, and more than 100% of the NASDAQ gains, have occurred when the NASDAQ was leading. More on this indicator can be found in the Market Timing Course, or on its page (which can be found by clicking on the chart on the charts page). <http://quantifiableedges.com/nasdaq-weekly-strength-model/>

I decided tonight to take a look at how the market has done when all 4 Market Timing Course indicators have been aligned as they are now. That means: 1) a leading NASDAQ, 2) SPX “Golden Cross” in effect, 3) favorable Presidential Cycle, and 4) “Worst” 6 months in effect. Below are stats showing SPX performance during this alignment.

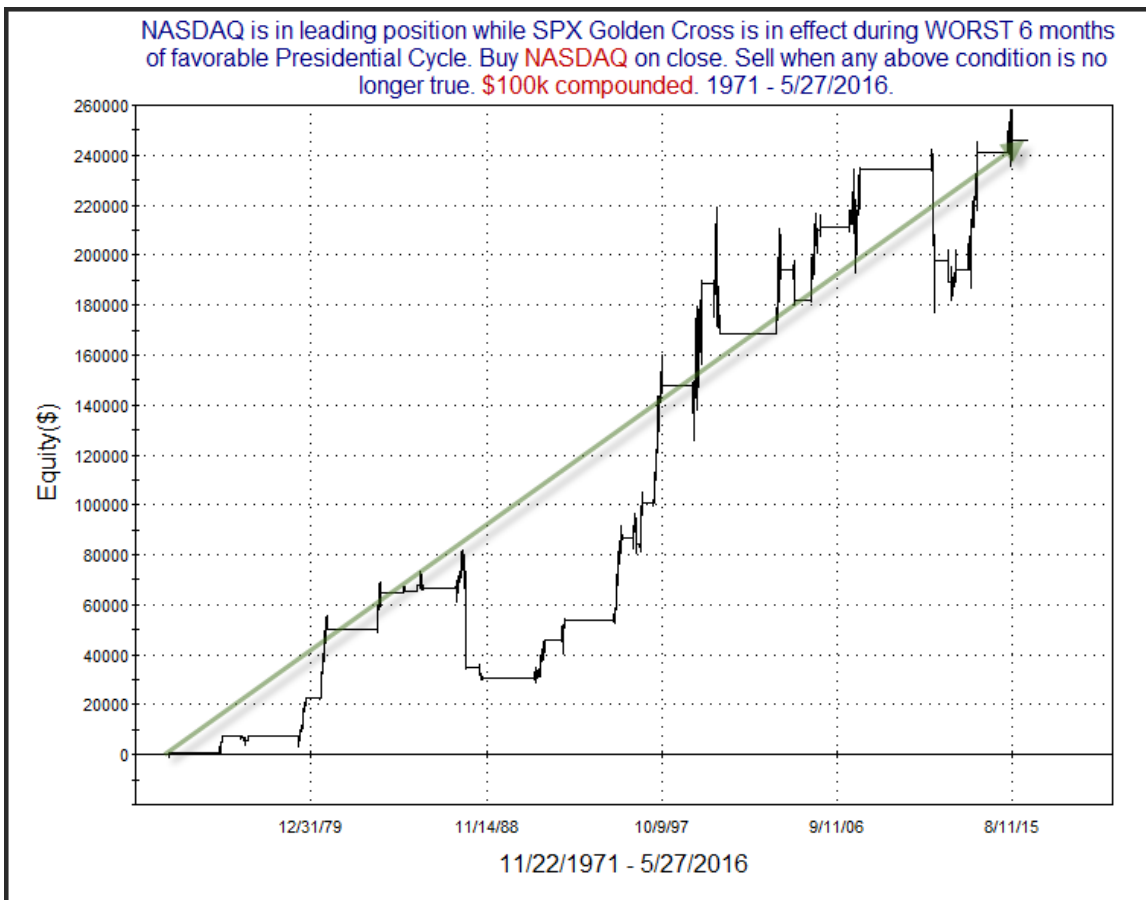
NASDAQ is in leading position while SPX Golden Cross is in effect during WORST 6 months of favorable Presidential Cycle. Buy SPX on close. Sell when any above condition is no longer true. \$100k/trade. 1971 - 5/27/2016.

TradeStation Performance Summary Expand ▾

All Trades

Total Net Profit	\$85,720.70	Profit Factor	2.65
Gross Profit	\$137,718.73	Gross Loss	(\$51,998.03)
Total Number of Trades	52	Percent Profitable	75.00%
Winning Trades	39	Losing Trades	13
Even Trades	0		
Avg. Trade Net Profit	\$1,648.47	Ratio Avg. Win:Avg. Loss	0.88
Avg. Winning Trade	\$3,531.25	Avg. Losing Trade	(\$3,999.85)
Largest Winning Trade	\$13,739.66	Largest Losing Trade	(\$20,174.85)

Stats here appear nicely favorable as this alignment has shown some strong gains over the years. Gross gains have been over 2.5 times the size of gross losses. Of course we learned in the Market Timing Course that when the NASDAQ was leading, it also generally continued to outperform the S&P 500. That holds true in this case as well. For the chart below I decided to look at buying the NASDAQ under these conditions. I also looked at compounding the returns rather than investing a flat \$100k/trade.

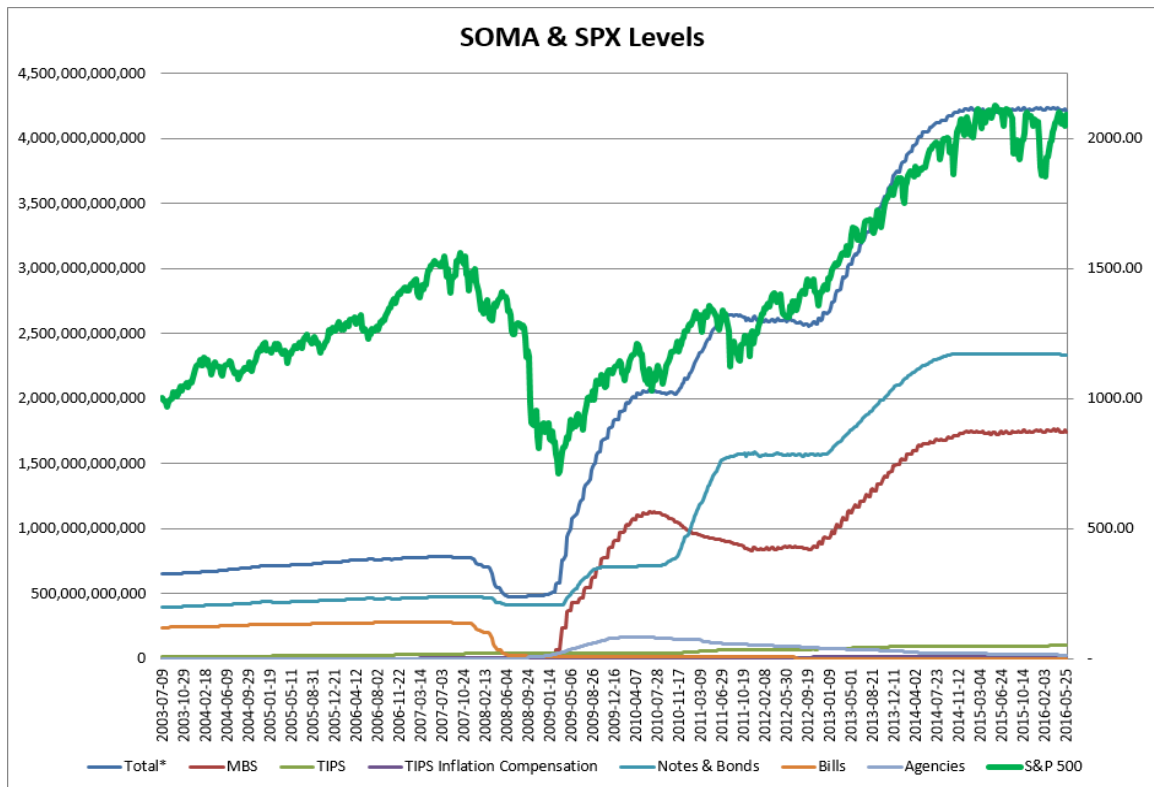


That's an impressive looking profit curve. The now-leading NASDAQ certainly appears to be good news for the bulls.

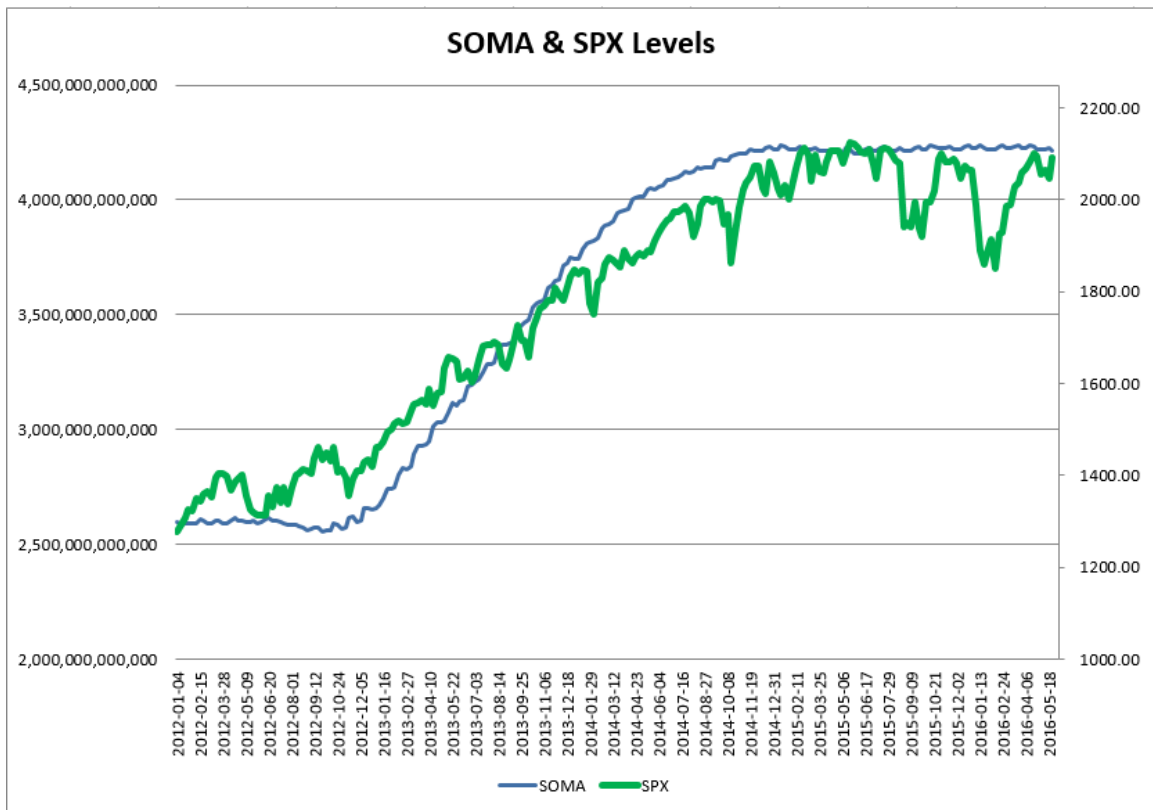
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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).



SOMA this past week (Wednesday to Wednesday) declined 0.28%. The declining SOMA is something I indicated was probable last week based on the Fed’s reinvestment schedule. The 2.10% gain for the SPX over this period is unusually strong. Most often the SPX will sell off during weeks that the SOMA does not expand. Since the beginning of 2015 SPX has risen 67% of the time for a sum total of 11.20% during SOMA expansion weeks. During all other weeks SPX has only risen 43% of the time and has lost a sum total of 8.42%. Based on the reinvestment schedule the Fed has stuck to over the last year and a half, this current week is likely to finish about flat. And the following week appears to be flat as well. So bulls are not likely to get any help from the Fed in the next week and a half.

It continues to be important to monitor SOMA activity, including the monthly reinvestment schedule so that we may quickly identify any change in policy and take steps to adjust our strategies. To this point the Fed has kept to their schedule of the last year and a half and we have not seen any strong derivations. I expect liquidity analysis to remain a vital tool for us.

Intermediate-term evidence remains mixed, but the bull case seems to be strengthening. Bears are counting on the weak Fed support, the “Worst 6 Months” and the long-term new-high breadth divergence. But 3 of the 4 Market Timing Course indicators are now bullish and that has generally been a strong positive for the market. Additionally, we have this week’s Inside Day study, the 20-low to 4-high study from last week, multiple breadth-thrust studies from February and the bullish FTD study from March. So with more and more favoring the bulls, I have moved my intermediate-term bias to “bullish”. Without any real Fed support, we could certainly see some gyrations here in the next few weeks. But a run at new all-time highs during June or July is looking more likely. With this bias my trades will primarily be long-focused, and it would take some very strong evidence to get me interested in shorts.

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