

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 2, 2018

Volume 11 Issue 1

Market Overview



Signals Overview

Aggregator	Aggressive VIX
Long	100% Long XIV

Tonight's Research Points

- A combination of factors is suggesting turn of the month is likely to see gains.
- SPY's big outside day reversal pattern suggests a short-term upside edge.
- The 1st dip below the 10ma for SPY after spending at least 25 days above it has typically been buyable.
- SOMA declined this past week and finished December down about \$5 billion.

Short-term Outlook

The Bottom Line

The Aggregator is again bullish. The market is short-term oversold. I am partially long, and may add more long exposure if there is further selling on Tuesday.

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						
January 2, 2018	EOM<10ma, Down, Bottom 1/2 range	1-2 days	Bullish			
January 2, 2018	3-day high, 3-day low 3-low close	1-5 days	Bullish			
January 2, 2018	SPY 1st close < 10ma in 25+ days	1-4 days	Bullish			
December 29, 2017	Gap up and partial reverse 2x	1-5 days	Bullish	1.70%	-0.70%	-1.30%
December 20, 2017	Twos 3 Nights Before Christmas	1-8 days	Bullish	2.50%	-1.10%	-2.20%
Active - Long Term						
January 2, 2018	SPY 1st close < 10ma in 25+ days	1-19 days	Bullish	4.10%	-0.90%	-2.15%
November 30, 2017	SPX 50-intraday high. NDX big down 50	1-50 days	Bullish			
November 29, 2017	SPX breaks 50-day Upper Bollinger Band	1-50 days	Bullish	4.85%	-4.10%	-7.80%
November 14, 2017	SPX top 25% 20day rng. RUT bottom 25	1-40 days	Bullish	5.60%	-2.80%	-5.50%
November 13, 2017	Hindenburg Omen Cluster	1-35 days	Bearish			
October 24, 2017	SPX 20-high. NDX big drop	1-50 days	Bullish	6.30%	-2.80%	-5.50%
October 2, 2017	SOMA reduction begins	int term	Bearish			
April 26, 2016	Golden Cross	int term	Bullish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			
Dropped Tonight						
December 20, 2017	Unfill gap up. Gap up reverse down.	1 day	Bullish			
December 19, 2017	VIX up. SPX 50-high. 1st day of week.	1-2 days	Bearish			

The Evidence

A positive year ended on a down note Friday. The SPX fell 0.5%, the NASDAQ lost 0.7%, and the Russell 2000 dropped 0.9%. Breadth was negative as the NYSE Up Issues % was 40% and the Up Volume % came in at 33%. NYSE volume rose some but was still holiday-light.

Several studies related to turn of the month triggered in the Quantifinder. Beginnings of new months often arrive with seasonal strength. This has especially been true 1) during long-term uptrends, 2) when the market is experiencing a short-term pullback, and 3) when it closes weakly on the last day of the month. In the study below I took these concepts and combined them. The study was last seen in the 8/1/17 letter. The very strong results have all been updated.

Today is the last trading day of the month. SPY closes > 200ma and positive on the month. It also closes < 10ma, down on the day, and the lower 50% of its intraday range. 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
5	38,866.56	29	23	6	79.31	2,105.06	5,025.88	-1,591.62	-6,349.55	1.32	5.07	1,340.23
4	34,890.15	29	22	7	75.86	1,881.40	3,718.84	-928.66	-4,936.67	2.03	6.37	1,203.11
3	31,986.42	29	23	6	79.31	1,599.63	4,245.00	-800.84	-1,673.59	2.00	7.66	1,102.98
2	28,499.84	29	28	1	96.55	1,056.60	3,135.34	-1,084.89	-1,084.89	0.97	27.27	982.75
1	22,539.80	29	27	2	93.10	850.88	1,792.50	-216.95	-257.40	3.92	52.95	777.23

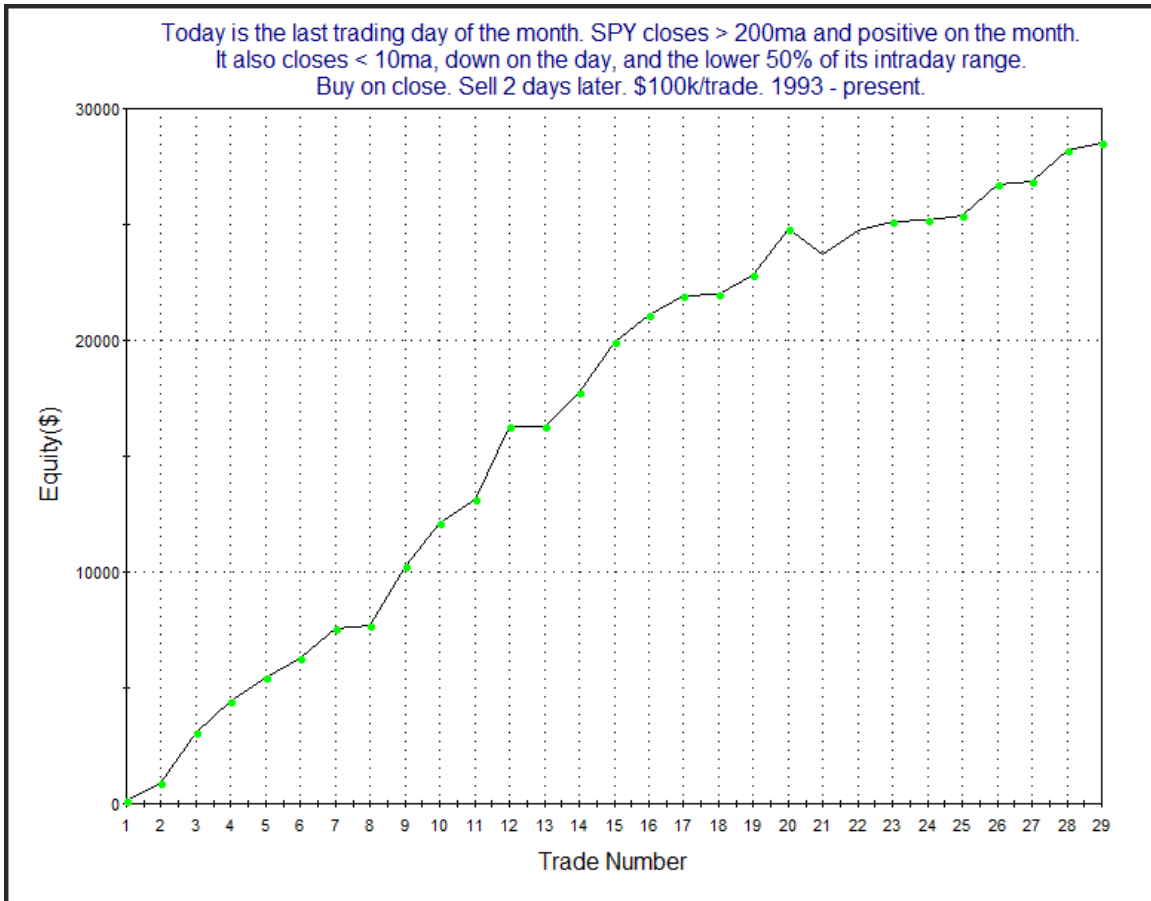
**The lone 2nd day loser DID close higher on Day 1.
It triggered on 4/30/10.**

The reliability of a bounce over the next 1-2 days has been remarkable. So were the 2-day Run-up/Drawdown stats, which I have pasted below:

Today is the last trading day of the month. SPY closes > 200ma and positive on the month. It also closes < 10ma, down on the day, and the lower 50% of its intraday range. Buy on close. Sell 2 days later. \$100k/trade. 1993 - present.

Run-up/Drawdown	Run-up	Drawdown
Max. Value	\$3,275.38	(\$1,589.49)
Max. Value Date	4/5/1999	5/4/2010
Avg. Value	\$1,472.29	(\$348.51)

The Avg Run-Up was nearly the size of the MAX Drawdown, and over 4x the size of the Avg Drawdown. Those are some impressive numbers. Here also is a profit curve.

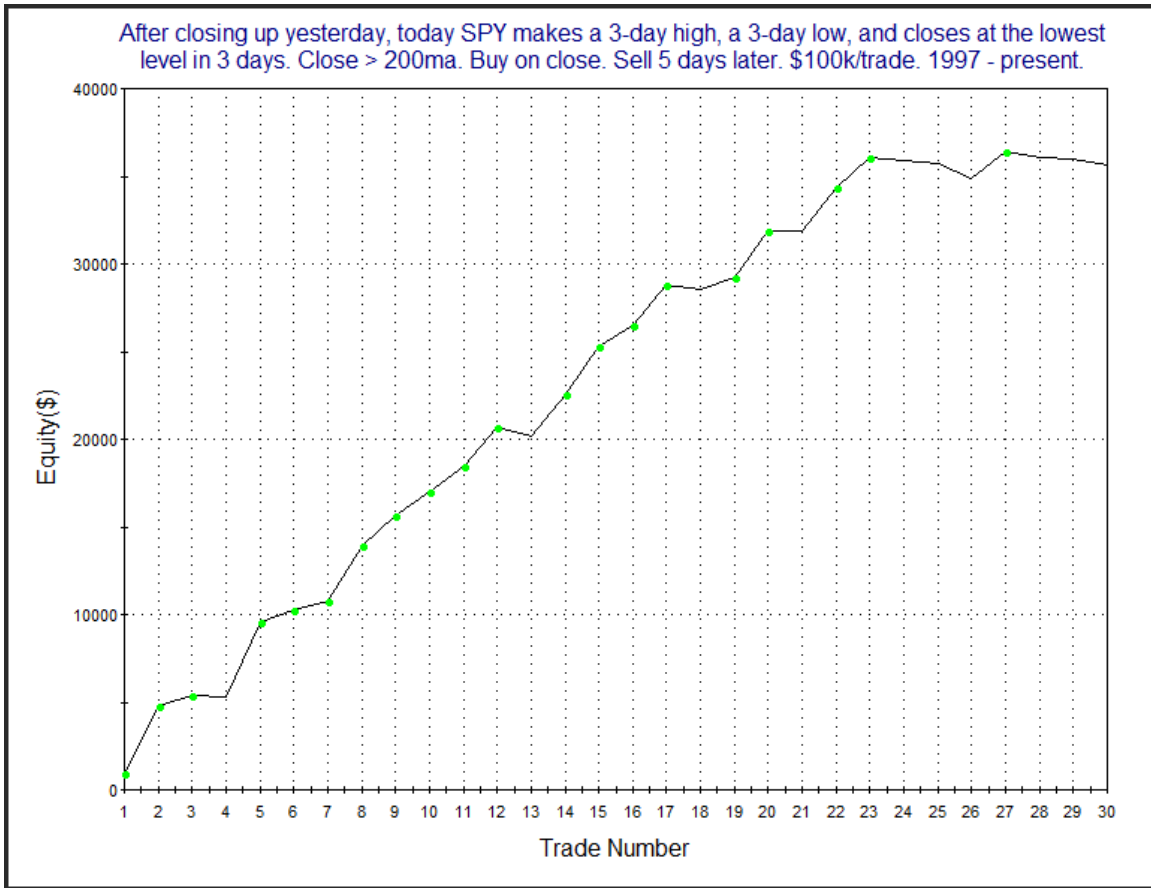


Other than the 1-instance hiccup, it has been a steady ride higher. This study certainly seems worthy of consideration.

SPY traded in a relatively wide range and closed down on Thursday. The study below was last shown in the 8/9/17 subscriber letter. It looks for the reversal day to engulf both of the last two days, close at a three-day low, and still be above the 200ma. All results are updated.

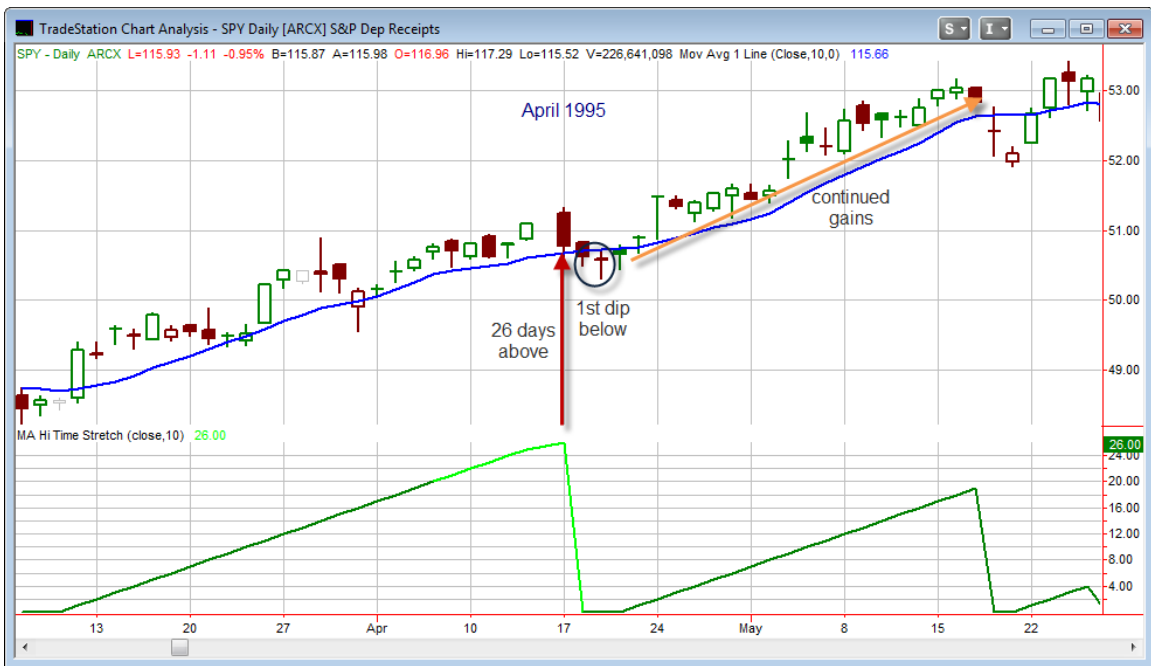
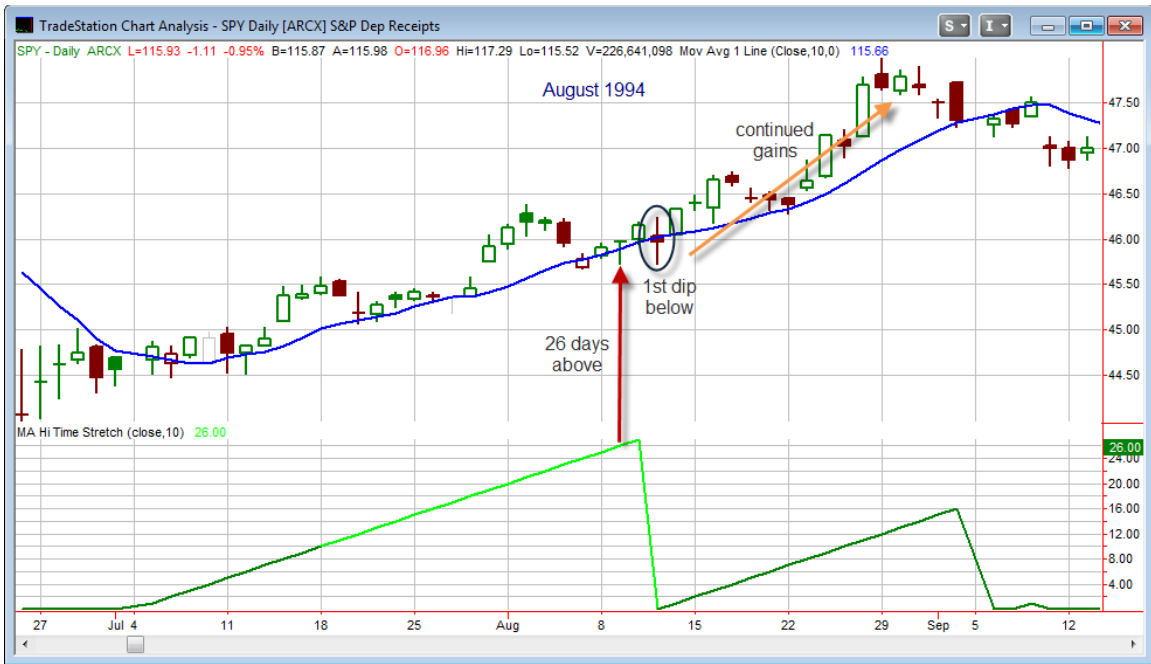
After closing up yesterday, today SPY makes a 3-day high, a 3-day low, and closes at the lowest level in 3 days. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1997 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	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	35,669.42	30	20	10	66.67	1,925.41	4,273.50	-283.87	-892.80	6.78	13.57	1,188.98
4	22,535.63	30	20	10	66.67	1,502.75	4,533.98	-751.94	-2,123.52	2.00	4.00	751.19
3	6,973.11	30	19	11	63.33	1,259.46	3,903.34	-1,541.51	-3,393.78	0.82	1.41	232.44
2	4,414.51	31	17	14	54.84	1,174.85	3,244.78	-1,111.28	-3,737.28	1.06	1.28	142.40
1	993.66	31	18	13	58.06	635.42	2,359.84	-803.38	-3,909.03	0.79	1.10	32.05

After the first couple of days there appears to be a strong and consistent upside edge. It is notable that with 29 instances, the biggest loser when looking out 5 days was less than 0.9%. Below is a profit curve that assumes a 5-day holding period.

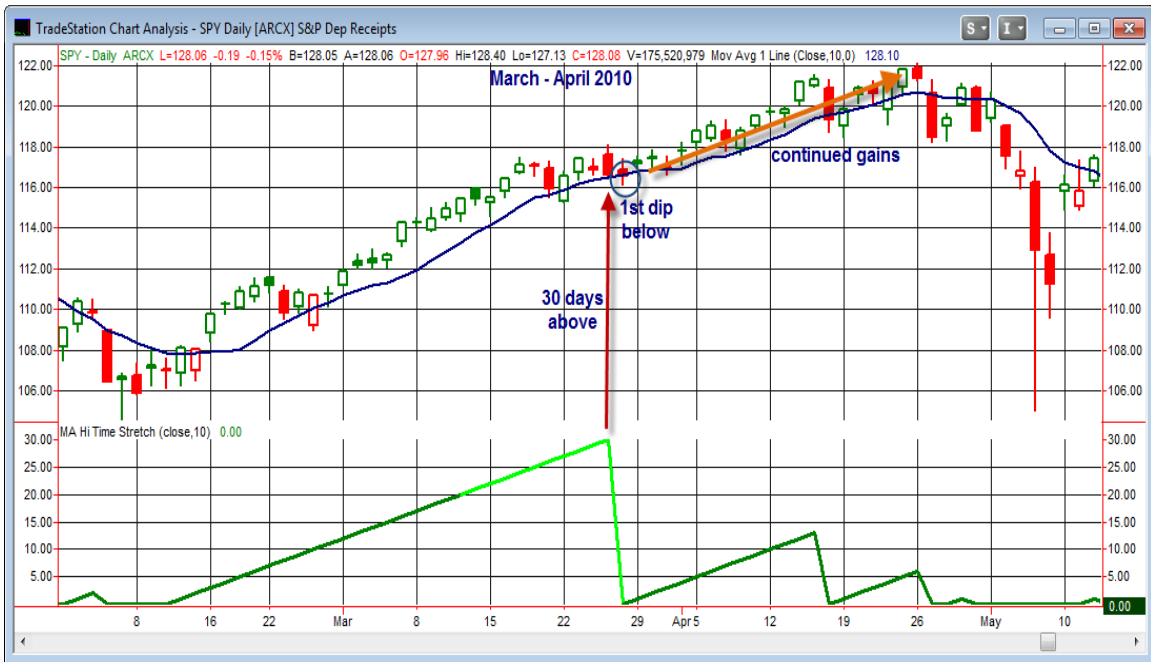


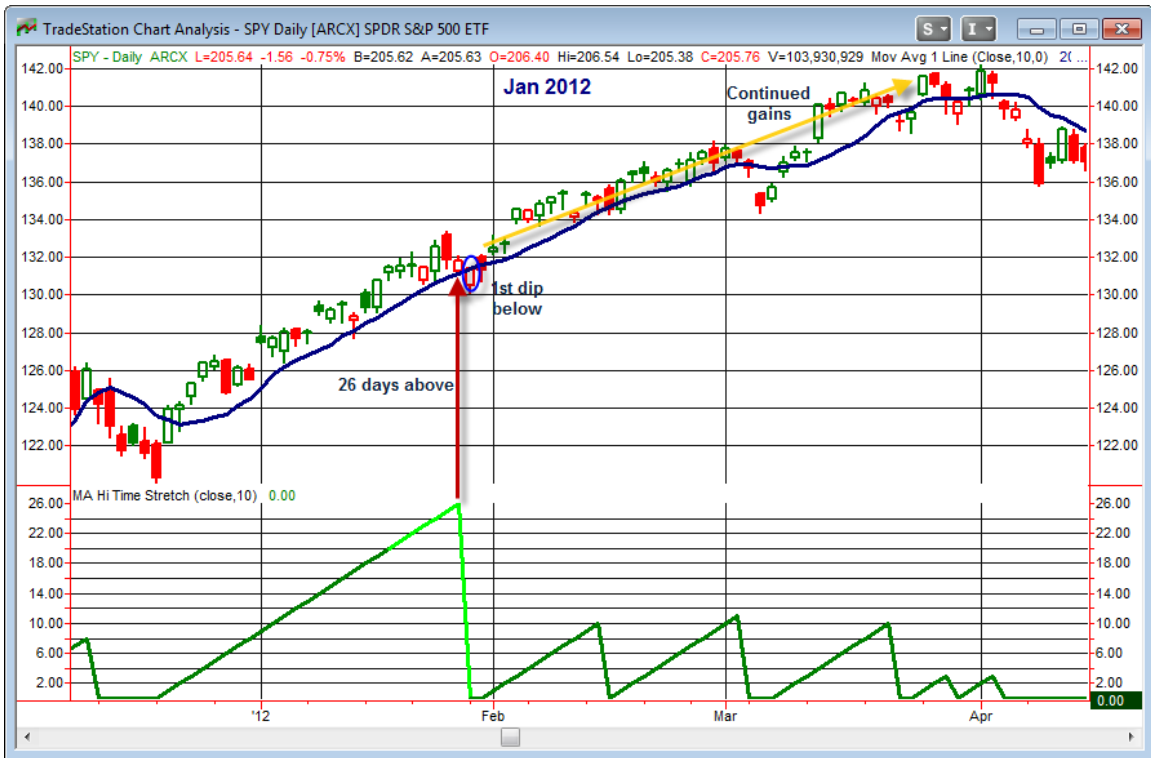
While the curve has flattened some lately, it still appears strong enough to suggest the upside edge is real. I have included this study on the Active List.

Another notable about Thursday's action is that the SPY closed below its 10ma for the first time since November 17th. In the 3/28/16 Subscriber Letter I looked at all the instances where SPY had traded above its 10ma for at least 25 days then closed below it. Since its inception in 1993 there have been only eleven other instances where SPY had a run of 25 days or more. I showed the charts of every instance and noted how the market reacted after it finally did close beneath its 10ma. Below I have republished those charts and added another one to show the most recent instance. The indicator in the bottom pane of each chart shows the number of days the SPY has closed above its 10ma.













Most of these charts look quite positive. Except for the November 2015 instance, the first trip below the 10ma was a short one, and the uptrend managed to reassert itself. Of course, if you've been reading Quantifiable Edges for any period of time, you're probably used to looking at numbers. So below you will find the stats table.

After closing above the 10ma for at least 25 days in a row, SPY closes below it today.
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
20	35,820.82	11	10	1	90.91	3,636.32	7,915.86	-542.40	-542.40	6.70	67.04	3,256.44
19	36,688.00	11	11	0	100.00	3,335.27	6,866.19	0.00	0.00	100.00	100.00	3,335.27
18	32,771.36	11	11	0	100.00	2,979.21	5,903.19	0.00	0.00	100.00	100.00	2,979.21
17	29,382.75	11	10	1	90.91	3,056.83	5,537.25	-1,185.60	-1,185.60	2.58	25.78	2,671.16
16	31,676.40	11	11	0	100.00	2,879.67	5,662.44	0.00	0.00	100.00	100.00	2,879.67
15	32,080.15	11	11	0	100.00	2,916.38	6,047.64	0.00	0.00	100.00	100.00	2,916.38
14	30,997.12	11	11	0	100.00	2,817.92	6,115.05	0.00	0.00	100.00	100.00	2,817.92
13	33,371.78	11	11	0	100.00	3,033.80	6,500.25	0.00	0.00	100.00	100.00	3,033.80
12	26,128.47	11	10	1	90.91	2,805.79	5,604.66	-1,929.42	-1,929.42	1.45	14.54	2,375.32
11	22,258.14	11	10	1	90.91	2,607.32	5,845.41	-3,815.10	-3,815.10	0.68	6.83	2,023.47
10	20,142.76	11	10	1	90.91	2,318.03	5,325.39	-3,037.50	-3,037.50	0.76	7.63	1,831.16
9	17,718.99	11	10	1	90.91	2,008.58	4,882.41	-2,366.82	-2,366.82	0.85	8.49	1,610.82
8	18,275.82	11	10	1	90.91	1,903.88	4,574.25	-763.02	-763.02	2.50	24.95	1,661.44
7	13,409.14	11	10	1	90.91	1,467.27	4,304.61	-1,263.60	-1,263.60	1.16	11.61	1,219.01
6	11,557.92	11	8	3	72.73	1,657.39	3,158.64	-567.06	-1,252.80	2.92	7.79	1,050.72
5	13,794.25	11	9	2	81.82	1,714.85	3,466.80	-819.72	-1,180.80	2.09	9.41	1,254.02
4	12,218.36	11	10	1	90.91	1,487.76	3,158.64	-2,659.20	-2,659.20	0.56	5.59	1,110.76
3	9,198.40	11	10	1	90.91	1,075.36	2,744.55	-1,555.20	-1,555.20	0.69	6.91	836.22
2	6,705.70	11	9	2	81.82	789.17	1,656.36	-198.40	-233.60	3.98	17.90	609.61
1	4,455.17	11	8	3	72.73	581.30	1,974.15	-65.07	-98.75	8.93	23.82	405.02

Strong and persistent upside movement like we have seen lately hasn't normally just ended and lead to an immediate correction. The 1st dip has most often been just that – a dip. New highs were typically made in short order. Of course the November 2015 instance was a big failure, and there is always a chance we could see that happen again. But the failure there was almost immediate. It did make some brief forays above the entry area, but it never moved to a new high, and the steep drop beyond the initial 10ma cross seemed to provide us a decent clue. In the 11/16/15 letter I wrote *“The persistency study from above would seem to help the bull case some – although the current instance has already misbehaved compared to all the rest. So perhaps that is a warning sign in itself.”* Overall I think this study is worth consideration. But if the market fails to act according to norms over the next few days, that will ring a warning bell for me.

I have updated the Aggregator chart below.



With tonight's studies considered, the green Aggregator Line again remained above zero. 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 SPX is oversold versus recent expectations. So expectations are positive and 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.

Based on the current active list, expectations are slated to remain bullish on Tuesday. This is unlikely to change, and would take very compelling bearish evidence to emerge to do so. The Differential Pivot will be 2692.76 on Tuesday. That is about 0.7% above Friday's close. Therefore, SPX will need to close up 0.7% on Tuesday in order to change from oversold to overbought versus expectations.

The Aggregator is bullish. New evidence is encouraging. The SPX has finally pulled back a fair amount, seasonality remains positive for the next few days, and there is ample room to the upside before SPX would turn from oversold to overbought. All in all, I like the setup. I took some long exposure at the close on Friday in SPY. I would note that QQQ is even more oversold. And if QQQ struggles on Tuesday, I will look to add some more exposure with QQQ.

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

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

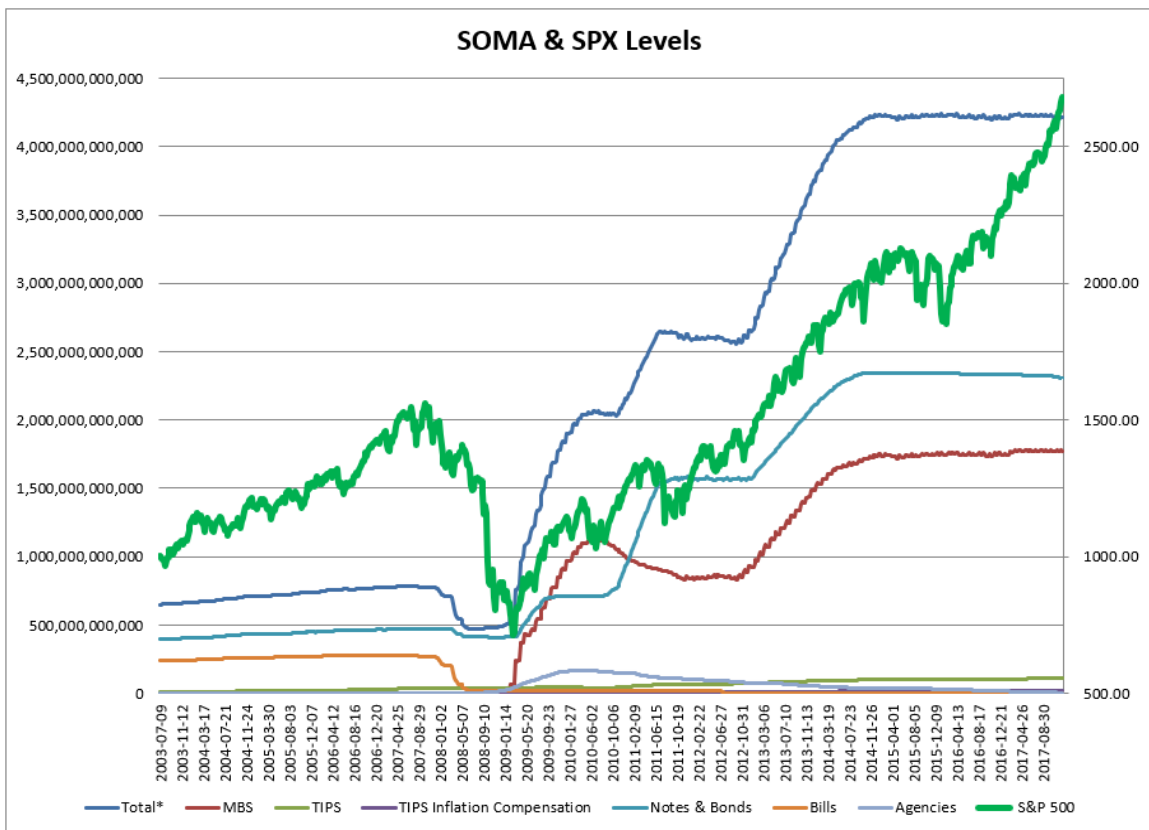
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#), 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.) *This week Combo System #3 stayed “Flat”, while the other 2 remained “Long”.*

This was a pullback week for the market, as most indices made lower highs, lows, and closes versus the previous week. Still, the selling was not steep. SPX only closed down about 0.4% from the previous week. Other than the “1st drop below the 10ma in over 25 days” study shown in the short-term section above, there were no additional studies that emerged with intermediate-term implications.

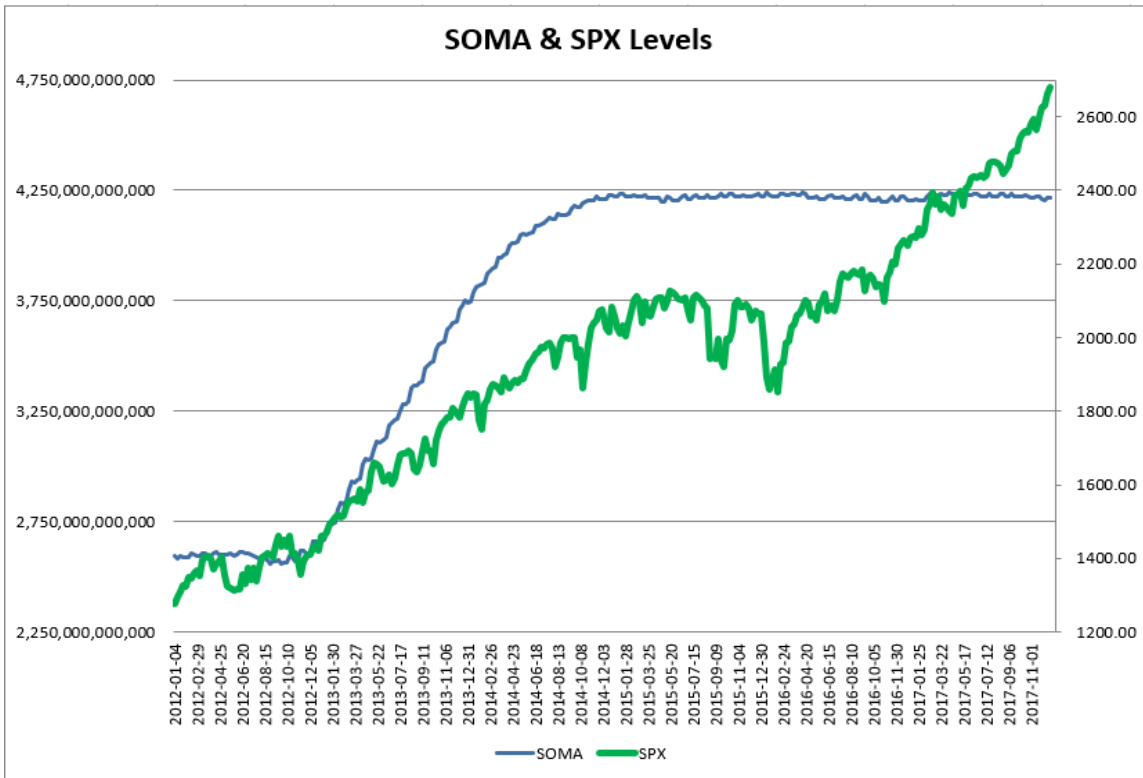
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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.

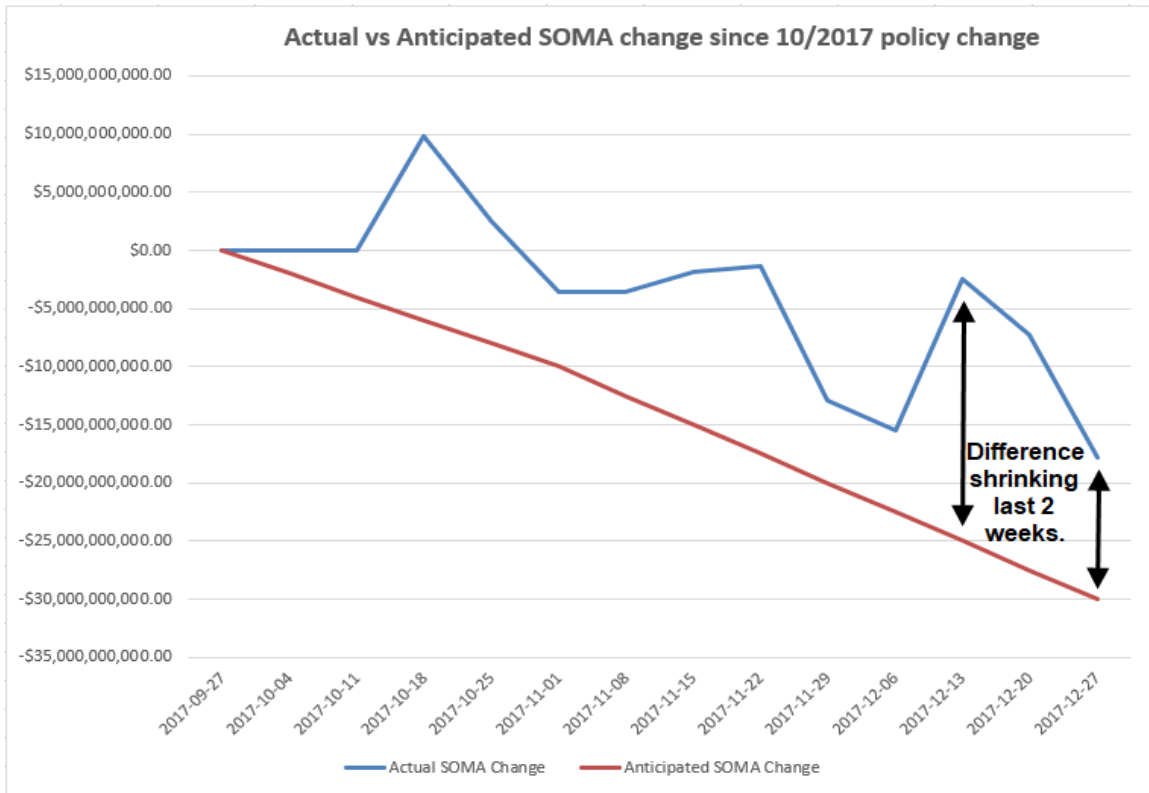
While the Fed is not making new QE purchases any longer, it is continuing to reinvest maturities. Therefore, the total assets in their System Open Market Account (SOMA) has not begun to dive like the old Quantifiable Edges POMO indicators did. Below are long and short-term views of SOMA and SPX. First,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



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



The Fed’s SOMA this past week (Wednesday to Wednesday) saw a reduction of about \$10.5 billion, or 0.25%. This leaves it net negative about \$4.9 billion for December. In September the Fed announced they would be reducing the SOMA at a rate of about \$10 billion per month starting in October. But in the 2.5 months since the start of October the SOMA has only declined a total of \$17.8 billion. The last 2 weeks we have seen fairly sizable declines as the reduction has perhaps been trying to play a little catch-up. As we can see in the charts, the market has typically done well when the Fed has expanded the SOMA and it has struggled when there have been substantial contractions. A few weeks ago, I created a chart that shows actual SOMA changes versus anticipated since the beginning of October based on the stated Fed policy.



It did play some catch-up the last couple of weeks, but it remains far off the pace overall. I will continue to watch the SOMA growth/shrinkage to see if it continues to shrink on a consistent basis. If that happens, it could provide a headwind for the bulls.

Overall evidence still appears to be favoring the bulls. There are several intermediate-term bullish studies that remain active, including the newest one from above. We are still in a period of strong seasonality. Additionally, the trend is still up, and 2 of 3 Market Timing Course Combo Systems are “long”. On the downside, the Hindenburg Omen signals remain. Of course Fed policy, and its implications, are still my biggest concern. There are no signs of a market correction starting just yet. My outlook is again somewhat bullish, and basically unchanged from last week. I will therefore continue to be a bit more aggressive with long trades and a bit more conservative when considering short trades.

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

Open Catapult Triggers

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.

QQQ – buy ¼ index position @ \$155.75 LIMIT ON CLOSE. Based on the short-term outlook above. There appears to be an upside edge, and QQQ looks especially oversold. If it closes down again on Tuesday, I will be a buyer.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	12/29/2017	\$266.86	\$266.86	0.00%		bought on close

A complete list of *Quantifiable Edges* trade idea results since the inception of the letter in 2008 [can be found here](#).

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