

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 22, 2018

Volume 11 Issue 14

Market Overview



Signals Overview

Aggregator	Aggressive VIX
Flat	50% Long XIV

Tonight's Research Points

- Solid gains during opex week are often reversed the following week.
- Since 1933, new Fed chairs have been met with some market enthusiasm in their first 3 weeks.
- The SOMA expanded this past week, and will need to decline fairly sharply the next few to see expected reductions get back on track.

Short-term Outlook

The Bottom Line

The Aggregator is neutral and so am I. Just not seeing a strong short-term edge at this point.

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 22, 2018	Opex Fri. SPX up 1%-2% last 5 days.	1-4 days	Bearish	-1.10%	0.75%	1.50%
January 17, 2018	VIX up > 10%. SPX down < 1%	1-5 days	Bullish			
January 16, 2018	SPX 50-high. VIX up. Friday	1-5 days	Bearish			
January 10, 2018	SPX > Bollinger Band 4 days	1-8 days	Bullish	2.00%	-1.30%	-2.70%
Active - Long Term						
January 16, 2018	NASDAQ Leading	int term	Bullish			
January 8, 2018	1st 4 days of year close higher	1-250 days	Bullish	15.90%	-5.70%	-11.10%
January 8, 2018	SOMA reduction intensifies to \$20 billion	int term	Bearish			
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%
April 26, 2016	Golden Cross	int term	Bullish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			

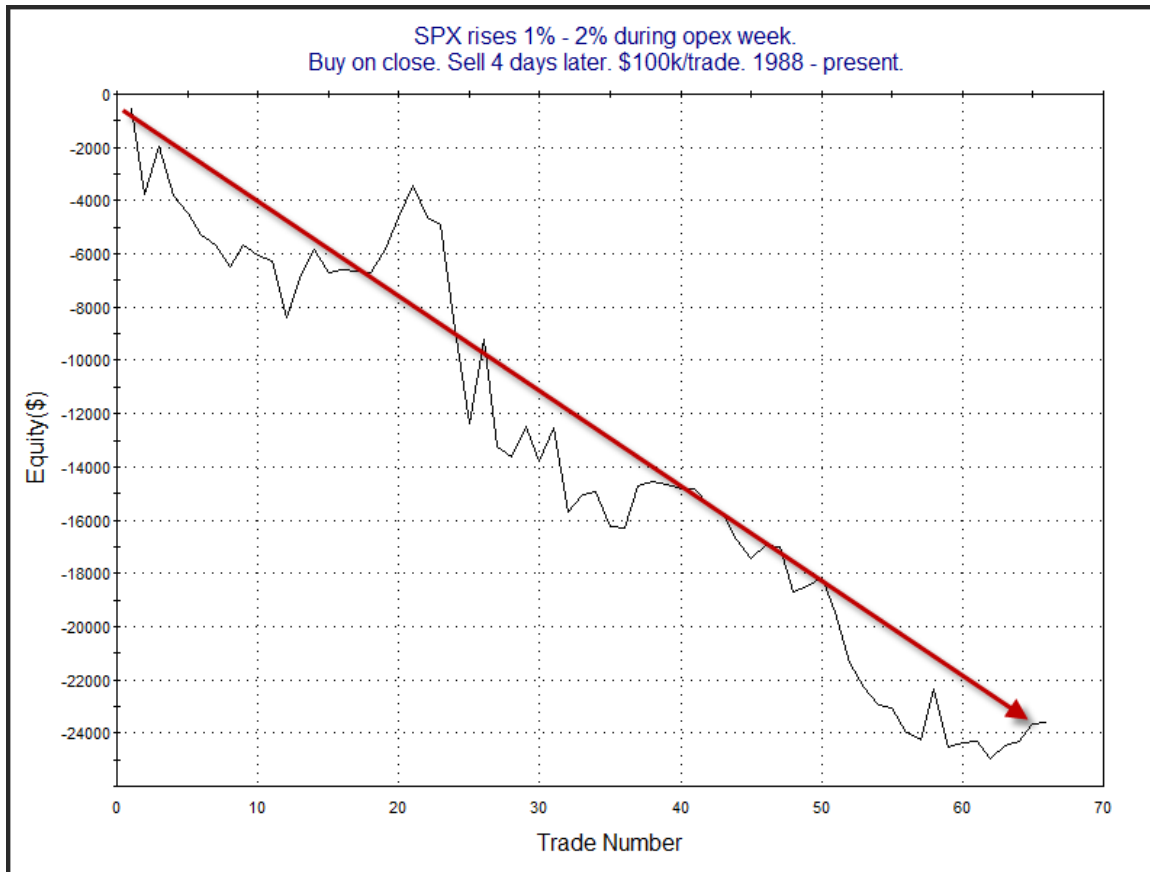
The Evidence

Thursday saw mild pullbacks for the indices. The SPX fell 0.2%, the NASDAQ dipped 0.03%, and the Russell 2000 lost 0.6%. Breadth was strongly negative as the NYSE Up Issues % was 28% and the Up Volume % came in at 34%. NYSE volume declined some from Wednesday's level.

The SPX posted solid gains on the week. Strong moves higher on opex week will often be followed by a pullback the following week. This is something we last saw in the 2/21/17 subscriber letter. I have updated the study from that letter below.

SPX rises 1% - 2% during opex week. Buy on close. Sell X days later. \$100k/trade. 1988 - 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	-25,342.66	66	27	39	40.91	1,004.96	3,146.64	-1,345.55	-4,961.56	0.75	0.52	-383.98
4	-23,618.06	66	25	41	37.88	848.12	3,212.16	-1,093.20	-4,046.70	0.78	0.47	-357.85
3	-5,399.50	66	33	33	50.00	761.31	3,403.68	-924.93	-2,765.00	0.82	0.82	-81.81
2	-8,208.77	66	34	32	51.52	549.11	1,590.30	-839.95	-2,917.60	0.65	0.69	-124.38
1	-4,038.39	66	29	37	43.94	480.08	1,739.10	-485.43	-2,470.65	0.99	0.78	-61.19

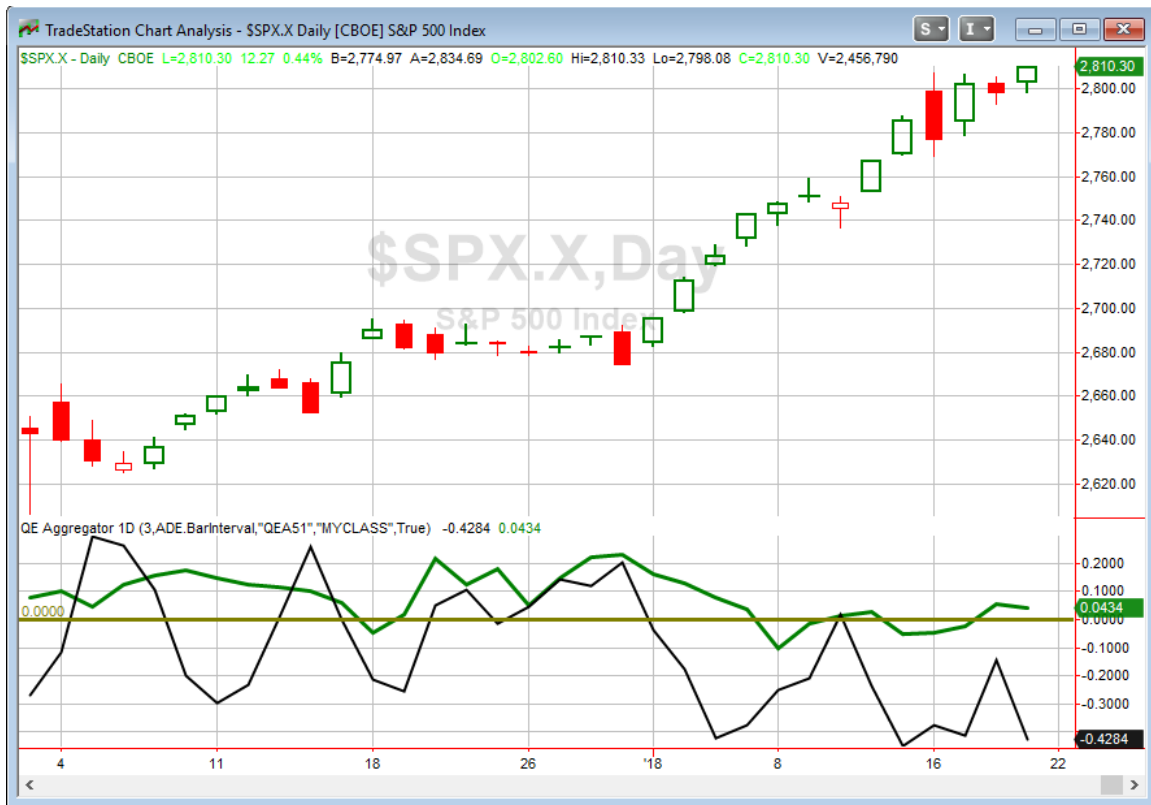
The stats suggest a short-term downside edge. Below is a profit curve assuming a 4-day holding strategy.



Despite the last few instances not panning out, this is an impressive curve. The downside edge has persisted for a long time. I have added this study to the Active List tonight.

There was another study that triggered which looked at SPY action over the last 3 days. The pattern of 50-day high close, then and inside day, then another 50-day high close had previously suggested bearish implications. But when I examined the study again tonight, I determined that the bearishness has waned significantly. I therefore decided not to include it in the letter. As we have seen this bull market persist over the last few years, the bulls have managed to trample a fair amount of evidence that at one time appeared bearish. That is not unusual or alarming. But it does underscore the need to constantly adapt to changing market conditions. This is why I update the Quantifiable Edges research and studies on a consistent basis.

I have updated the Aggregator chart below.



Even with the bearish study being added tonight the green Aggregator Line 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 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 stayed flat at the close.

Based on the current active list, expectations are set to turn bearish on Monday. This could change if compelling new bullish evidence emerges. The Differential Pivot will be 2799.17 on Monday. That is 0.4% below Friday's close. So SPX would need to close down at least 0.4% in order to flip from overbought to oversold versus recent expectations.

The market remains difficult for short-term swing trading. The constant push higher is leaving it too overbought to buy and too strong to short. Evidence is mixed, and is set to turn from a short-term bullish tilt to short-term bearish. The current state simply does not suggest strong reward/risk for either longs or shorts. I will remain patient until a better reward/risk opportunity comes along.

Fed Chairman Study Update

Jerome Powell is expected to take over for Janet Yellen as the new Fed chairman on Feb 3rd. A few days ago in the letter I looked at SPX performance after a new chairman takes over. I used the SPX and looked back to 1970. Tonight I decided to take the analysis back to 1923 using my Dow data. Like with the SPX, I found the first few weeks to be the most consistent and interesting data. Once we look out much further, the results become more mixed. So below is a list of past Fed chairman changes along with the 15-day performance of the Dow.

Buy Dow Jones Industrials at the close the day before a new Fed chairman takes over. Sell 15 days later. \$100k/trade. 1923 - present.				
Date/Time	Signal	Price	% Profit	Chairman
4/30/1923	Buy	\$98.40	-5.69%	Daniel Crissinger
5/21/1923	Sell	\$92.80		
9/30/1927	Buy	\$197.60	-8.20%	Roy Young
10/24/1927	Sell	\$181.40		
9/15/1930	Buy	\$236.60	-14.29%	Eugene Meyer
10/6/1930	Sell	\$202.80		
5/18/1933	Buy	\$82.60	14.16%	Eugene Black
6/9/1933	Sell	\$94.30		
11/14/1934	Buy	\$99.40	4.12%	Marriner S. Eccles
12/6/1934	Sell	\$103.50		
4/14/1938	Buy	\$116.80	0.34%	Thomas B. McCabe
5/6/1938	Sell	\$117.20		
3/30/1951	Buy	\$248.50	2.54%	William M. Martin
4/20/1951	Sell	\$254.80		
1/30/1970	Buy	\$744.10	1.80%	Arthur Burns
2/20/1970	Sell	\$757.50		
3/7/1978	Buy	\$746.80	2.01%	G. William Miller
3/29/1978	Sell	\$761.80		
8/3/1979	Buy	\$846.20	4.02%	Paul Volcker
8/24/1979	Sell	\$880.20		
8/10/1987	Buy	\$2,635.84	1.03%	Alan Greenspan
8/31/1987	Sell	\$2,662.95		
1/31/2006	Buy	\$10,864.86	2.51%	Ben Bernanke
2/22/2006	Sell	\$11,137.17		
1/31/2014	Buy	\$15,698.85	3.24%	Janet Yellen
2/24/2014	Sell	\$16,207.14		

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After 3 rough instances to begin the study, the rest of the chairman have been greeted with enthusiasm by the market in their early days. It did not always last. (Greenspan saw the crash of '87 after just a few months on the job.) But if the last ten chairmen are any indication, the market rally may continue into February. Or if the market decides it really does not like Mr. Powell, then a Eugene Meyer nosedive would make for a tough few weeks. Personally, this was more an exercise in curiosity, than anything I plan to base a big trade on. Good luck Mr. Powell! We hope you are met with at least as much enthusiasm as Thomas McCabe was.

Intermediate-term Outlook (2 weeks – 2 months) – updated 1/22– somewhat bullish

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

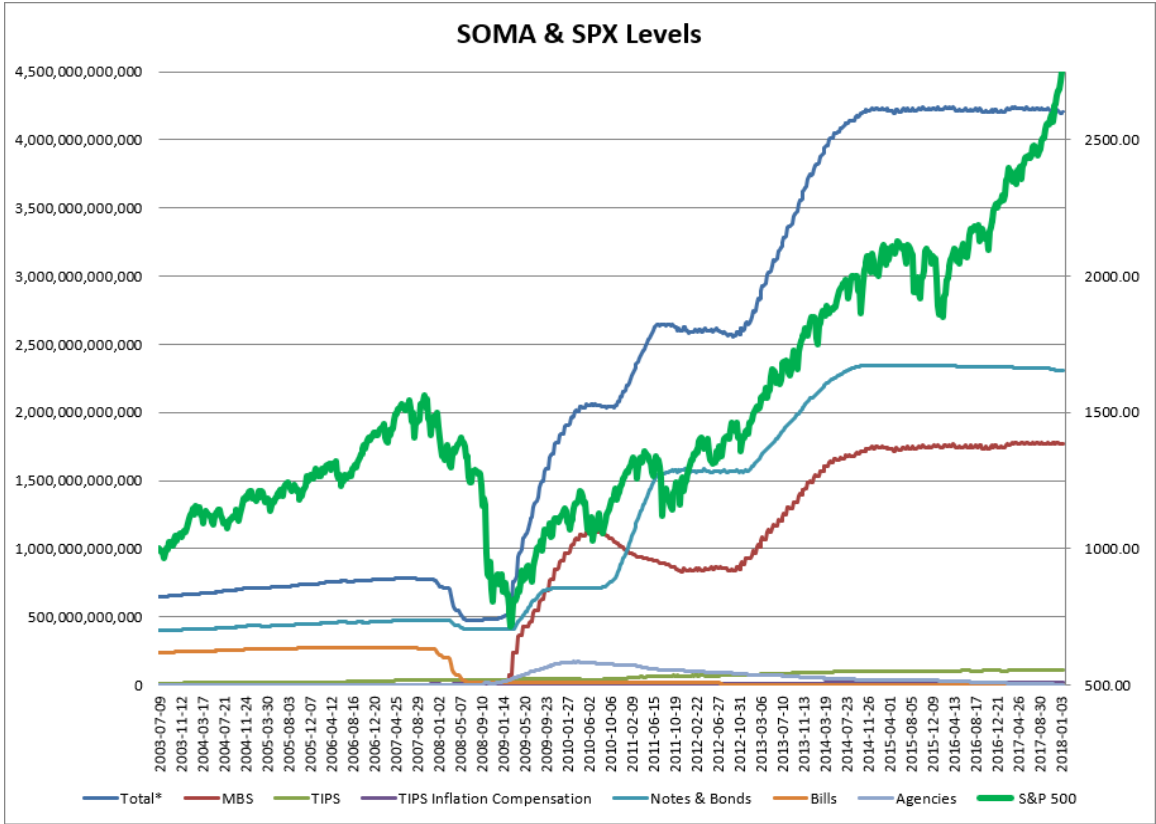
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#),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

The market continued to rally and again finished the week at new all-time highs. The SPX closed the week up 0.9% and the NASDAQ rose 1.0%. With most major indices closing at new all-time highs on Friday, there is little doubt the uptrend remains intact. Unfortunately, the move higher this week did not manage to generate any new and compelling evidence with intermediate-term implications.

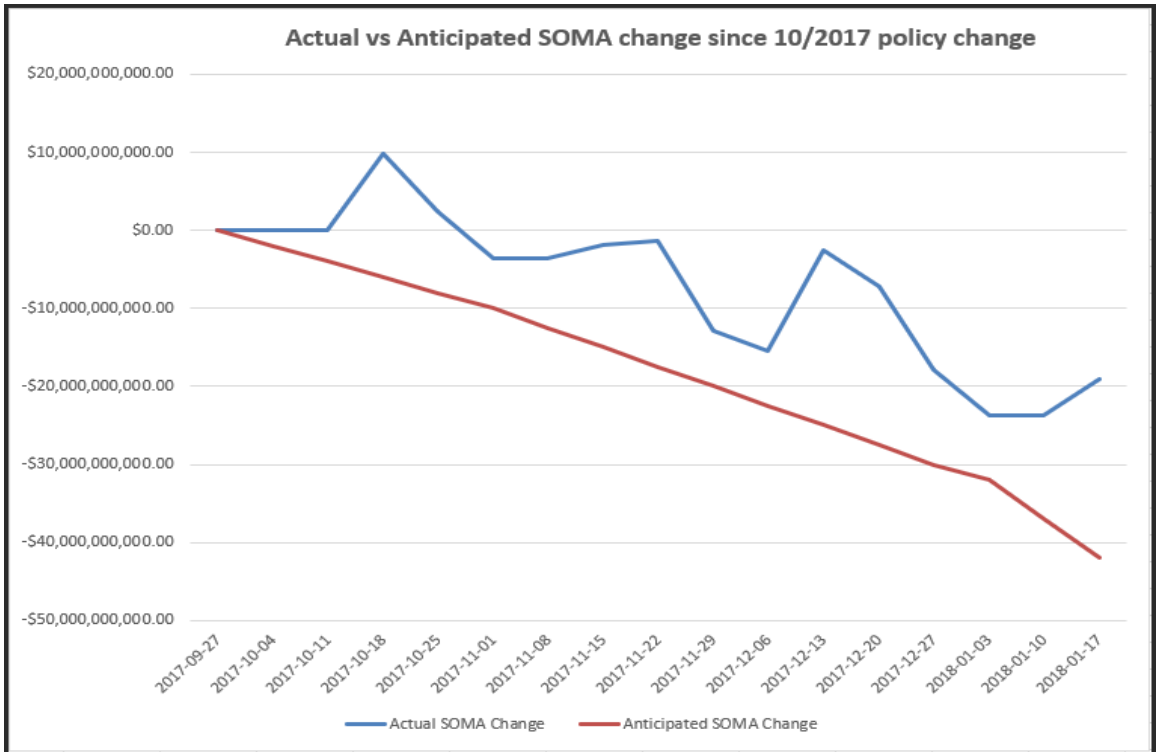
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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 a zoomed-in view since October comparing expected reductions to actual.



The Fed's SOMA this past week (Wednesday to Wednesday) actually increased nearly \$4.7 billion, or about 0.11%. With the Fed looking to lower the SOMA by about \$20 billion / month right now, that is a sizable difference from what is expected during a typical week. So the fact that the market has managed to push higher over the last 2 weeks with the SOMA actually rising is not a big surprise. If the Fed plan plays a little catch-up here late in the month, then that might act as a headwind. Up until now, the mild rate of reduction in the SOMA since October has not hindered the bull market. But each quarter this year the rate of decline is set to be upped by \$10 billion / month. So it could go to \$30 billion starting in April, and then \$40 billion in July and \$50 billion in October, where it is expected to remain and not increase further. Historically, the market has performed well during times of expansion, and it has struggled when the SOMA has shrank. While the rate of reduction has not caused a liquidity issue yet, I fully expect it will at some point. And 2018 will likely see corrections and volatility of greater magnitude than 2017. This could make trading more challenging, but it could also mean more opportunity for traders to make money – perhaps in both directions.

Overall evidence still appears to be favoring the bulls. There are several intermediate-term bullish studies that remain active. Additionally, the trend is still up, and all 3 Market Timing Course Combo Systems are “long”. Fed policy, and its implications, is still my biggest concern. There are no signs of a market correction starting just yet. My outlook is again somewhat bullish. I will continue to be a bit more aggressive with long trades and especially conservative when considering short trades.

Catapult and Capitulative Breadth Statistics

[*Catapult & CBI Presentation Link*](#)

Open Catapult Triggers

DUK -1/3 @ \$81.94 (bought 1/3 at limit)

DUK -1/3 @ \$79.28 (bought 1/3 at limit)

DUK -1/3 @ \$78.90 (bought 1/3 at limit)

Broad Market Large Cap CBI – 3(DUK-3)

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
DUK(1/3)	1/8/2018	\$81.94	\$76.82	-6.25%		Catapult
DUK(1/3)	1/12/2018	\$79.00	\$76.82	-2.76%		Catapult
DUK(1/3)	1/16/2018	\$78.90	\$76.82	-2.64%		Catapult

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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