

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

April 30, 2018

Volume 11 Issue 82

## Market Overview



## Signals Overview

Aggregator	CBI Reading
Flat	0

## Tonight's Research Points

- SPX up 3 days but below the close of 4 days ago is often followed by more upside.
- The Worst 6 Months is set to begin on Monday afternoon. Several studies show this could be a difficult summer.
- The SOMA saw a sizable reduction this past week, and should see a further decline this upcoming week, acting as a bearish influence on the market.

### *Short-term Outlook*

#### *The Bottom Line*

Short-term expectations remain bullish, but the market is now overbought. This leaves me neutral and awaiting the next favorable trading opportunity.

**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
<b>Active - Short Term</b>						
April 30, 2018	SPX up 3 but < 4 ago	1 day	Bullish			
April 27, 2018	10-low yest. Unfill gap up < 10 > 200ma	1-5 days	Bullish	1.80%	-1.20%	-2.20%
April 26, 2018	Higher then dn . Lower then up.	1-5 days	Bullish	1.80%	-1.20%	-2.40%
<b>Active - Long Term</b>						
April 23, 2018	1st 5-low in 10+ days. Close > 10ma.	1-10 days	Bullish	2.20%	-1.30%	-2.60%
April 6, 2018	2%+ gain over 3 days. Offset HV < 0.25	1-19 days	Bullish	4.30%	-2.20%	-4.80%
April 2, 2018	SOMA reduction intensifies to \$30billion	int term	Bearish			
February 15, 2018	FTD with moderate breadth & volume	int term	Bearish			
January 8, 2018	1st 4 days of year close higher	1-250 days	Bullish	15.90%	-5.70%	-11.10%
April 26, 2016	Golden Cross	int term	Bullish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			

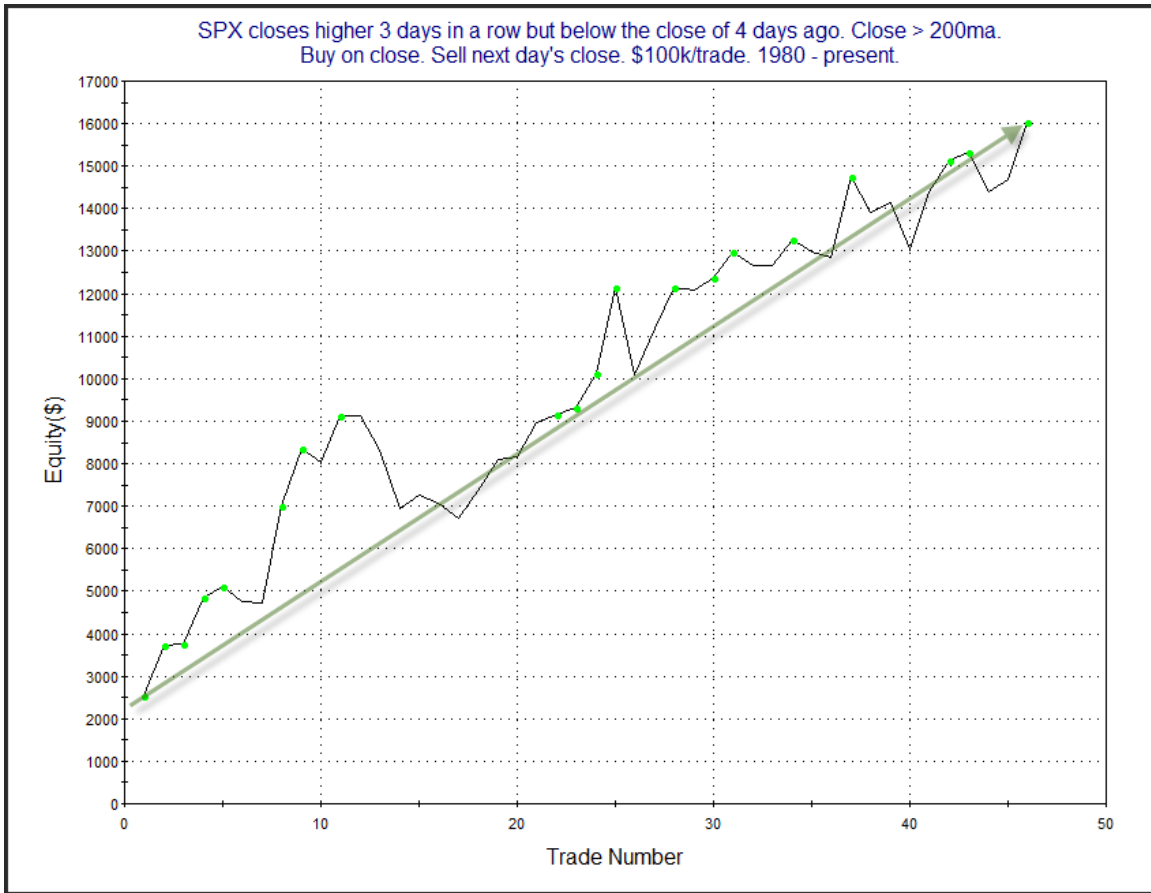
**The Evidence**

A big gap up did not hold very well and the market ended mixed. SPX closed up 0.1%, the NASDAQ rose 0.02% and the Russell 2000 declined 0.1%. Breadth was positive as the NYSE Up Issues % was 57% and the Up Volume % came in at 56%. NYSE volume came in very light.

Mild moves don't often lead to very compelling studies. One study from the Quantifinder tonight that I thought was worth considering was last shown in the 11/3/17 Subscriber Letter. It looked at 3-day rallies that could not overcome the 1-day drop that occurred 4 days ago. I have updated the results below.

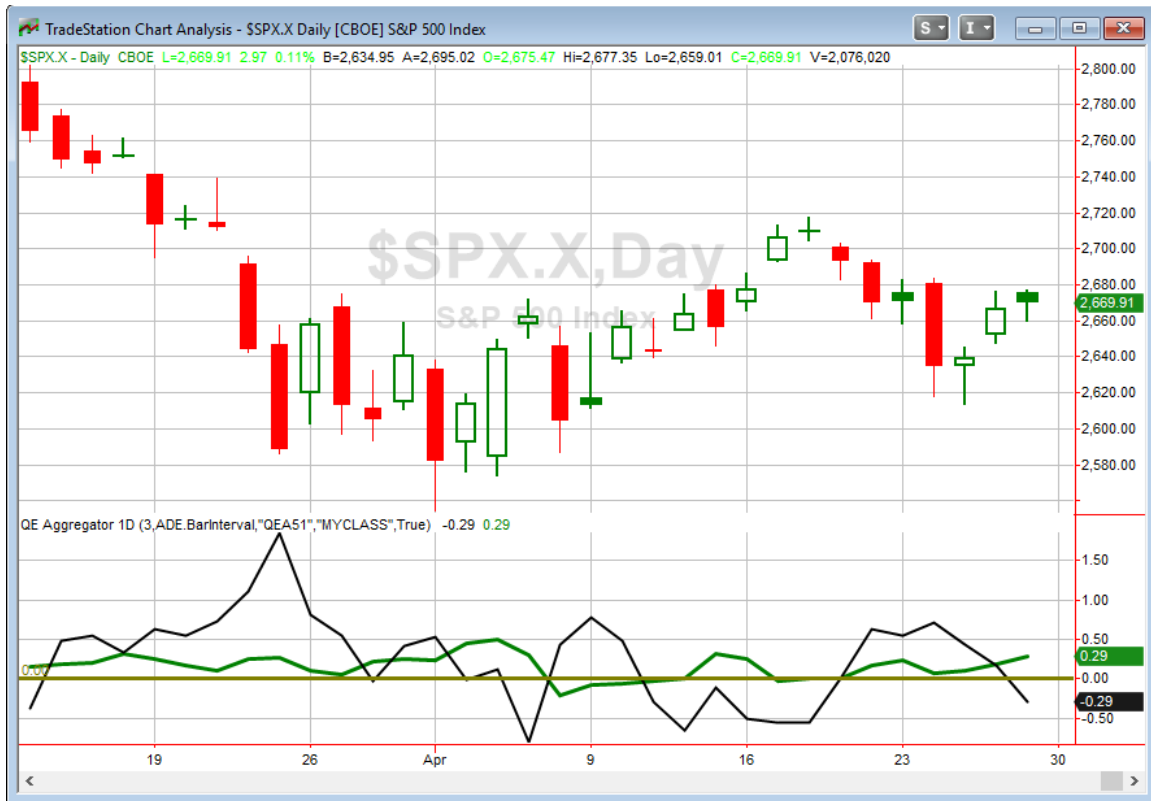
SPX closes higher 3 days in a row but below the close of 4 days ago. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1980 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	19,005.43	46	28	18	60.87	1,568.38	6,422.84	-1,383.84	-3,864.28	1.13	1.76	413.16
4	21,601.62	46	31	15	67.39	1,463.60	4,938.89	-1,584.67	-4,304.58	0.92	1.91	469.60
3	16,906.85	46	28	18	60.87	1,436.01	4,482.29	-1,294.52	-4,052.24	1.11	1.73	367.54
2	16,607.05	46	30	16	65.22	1,038.60	3,980.03	-909.43	-2,257.55	1.14	2.14	361.02
1	16,020.44	46	30	15	65.22	839.99	2,534.13	-611.95	-2,068.30	1.37	2.75	348.27

I found it interesting that despite the fact the market had already risen for 3 days in a row, the fourth day showed gains nearly 2/3 of the time. This even held true over the 1-4 day period, although most of the gains were realized on day 1. To see how this potential edge has played out over time I ran an equity curve using a 1-day hold.



The equity curve appears steady and solid, and continues to make new highs. I have included this study on the Active List tonight.

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



With tonight's new study included the green Aggregator Line again held above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line dipped 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.

Based on the current active studies, expectations are slated to remain bullish on Monday. Of course, this could change if compelling new bearish evidence emerges. The Differential Pivot will be 2650.13 on Monday. That is 0.7% below Friday's close. So SPX will need to close down 0.7% on Monday in order to flip from overbought to oversold versus expectations.

I took off my index exposure at the open on Friday, which turned out to be a fortunate exit time. With the remaining Catapults hitting their exit triggers, I will be looking to sell my exposure there at the open on Monday. While market expectations remain bullish, the overbought nature of the market leaves reward/risk less than desirable. I'll wait for the next favorable entry opportunity to emerge before heading back into the market.

**Intermediate-term Outlook (2 weeks – 2 months) – *updated 4/30– neutral turning to bearish on Friday***

Combo #1	Combo #2	Combo #3
Long (flat at Monday's close)	Long (flat at Monday's close)	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 there were no changes to the Combo Systems. *But at the close on Monday the “Worst 6 Months” will begin. This will leave the Golden Cross as the only positive Market Timing Course indicator, and will cause all 3 Combo Systems to change to flat.*

The SPX ended the week near breakeven, with a decline of just 0.23 points. The NASDAQ fell a little more with a 0.4% drop. There were no new studies that emerged with intermediate-term implications. But the changing of the calendar to May on Tuesday will put us in the “Worst 6 Months” period.

The “Worst 6 Months” has implications for a number of reasons. Last week I examined it in context of how the market had been acting up to that point in the year. Today I will also view it in relation to the current position of the other 3 QE Market Timing Course indicators. Lastly, I’ll show a study that examines potential volatility during the “Worst 6 Months” of an unfavorable Presidential Cycle year. First, here is a copy of the study I published last weekend.

*Over the last several years I have looked at the “Worst 6 Months” and filtered it by whether the market has suffered a pullback at any point leading up to the end of April. To define “pullback” I started with a clean slate every year on January 1. The high of Jan 1 was the high for the year as of that date. Each time a new high was made I would measure the pullbacks from the highest high to-date. I broke “Sell in May” down by years the SPX had a 5% pullback before May versus years it did not. Three-quarters of the time we have seen a 5% pullback. The updated results table below shows times where there had NOT been a pullback at some point before May.*

It is the last day of April. SPX has NOT pulled back > 5% at any point this year.  
Buy on close. Sell on close last day of October. \$100k/trade. 1961 - present.

TradeStation Performance Summary				Expand
<b>All Trades</b>				
Total Net Profit	\$68,300.42	Profit Factor	7.57	
Gross Profit	\$78,694.84	Gross Loss	(\$10,394.42)	
Total Number of Trades	16	Percent Profitable	81.25%	
Winning Trades	13	Losing Trades	3	
Even Trades	0			
Avg. Trade Net Profit	\$4,268.78	Ratio Avg. Win:Avg. Loss	1.75	
Avg. Winning Trade	\$6,053.45	Avg. Losing Trade	(\$3,464.81)	
Largest Winning Trade	\$12,957.26	Largest Losing Trade	(\$9,350.64)	

Results here are actually quite positive. They suggest that when there has been a strong market headed into May that the May-October period has been pretty good. Of course, this is not the case this year. In 2018 we have had a sizable pullback. And that leaves us looking at the study below.

TradeStation Performance Summary				Expand
<b>All Trades</b>				
Total Net Profit	(\$8,361.33)	Profit Factor	0.95	
Gross Profit	\$154,754.69	Gross Loss	(\$163,116.02)	
Total Number of Trades	41	Percent Profitable	58.54%	
Winning Trades	24	Losing Trades	17	
Even Trades	0			
Avg. Trade Net Profit	(\$203.93)	Ratio Avg. Win:Avg. Loss	0.67	
Avg. Winning Trade	\$6,448.11	Avg. Losing Trade	(\$9,595.06)	
Largest Winning Trade	\$19,909.20	Largest Losing Trade	(\$30,011.76)	
<p><b>Avg Run-up: 8.1% Avg Drawdown: -10.4%</b>  <b>15 of 41 years saw a drawdown of at least 10%,</b>  <b>and 7 of them finished with a loss of greater than 10%.</b></p>				

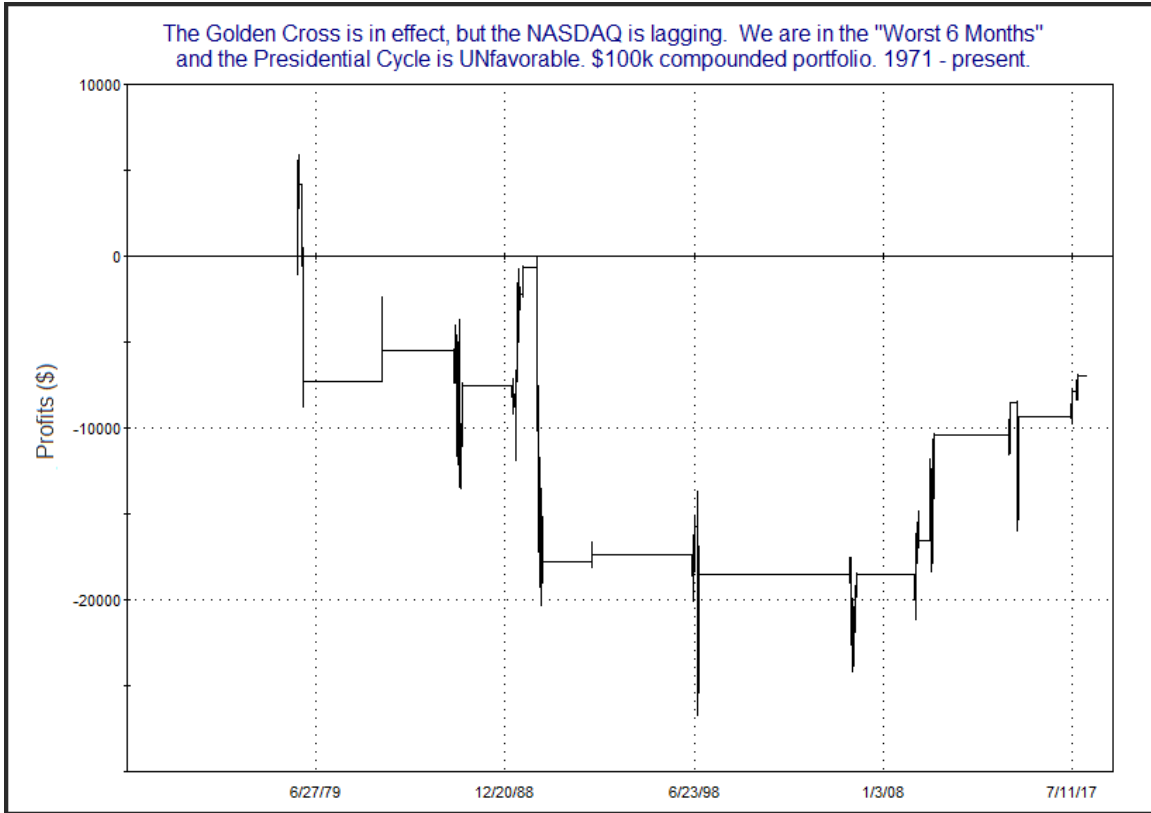
Of the 41 years where pullback had occurred, 15 of them saw the market drop more than 10% from its April closing price during the next 6 months. And 7 of them were more than 10% lower at the close of October. There were slightly more winning years than losing ones, but the losers were quite a bit bigger and the market has suffered net losses during the May – October period for these 41 years. This won't be in effect until the end of the month, but it appears the market could be susceptible to some poor seasonal influence over the May – October timeframe.

Of course, it is not just the “Worst 6 Months” that the market has to deal with. We are also in an unfavorable period of the Presidential Cycle. I detail the Presidential Cycle in the Quantifiable Edges Market Timing Course. As a brief intro, the cycle is unfavorable during the 1<sup>st</sup> year of a new president, and also during all 2<sup>nd</sup> years of a presidential term. We are currently in year 2 of Trump’s presidency, which leaves us in an unfavorable portion of the Presidential Cycle. So let’s now look and see how the SPX has performed when the Market Timing Course indicators have been in their current state.

The Golden Cross is in effect, but the NASDAQ is lagging. We are in the "Worst 6 Months" and the Presidential Cycle is UNfavorable. \$100k/trade. 1971 - present.

TradeStation Performance Summary <span style="float: right;">Expand ▾</span>			
All Trades			
Total Net Profit	(\$4,424.68)	Profit Factor	0.88
Gross Profit	\$31,576.06	Gross Loss	(\$36,000.74)
Total Number of Trades	27	Percent Profitable	70.37%
Winning Trades	19	Losing Trades	8
Even Trades	0		
Avg. Trade Net Profit	(\$163.88)	Ratio Avg. Win:Avg. Loss	0.37
Avg. Winning Trade	\$1,661.90	Avg. Losing Trade	(\$4,500.09)
Largest Winning Trade	\$6,311.04	Largest Losing Trade	(\$17,220.32)

The stats here are mostly poor, as the market has historically generated a net loss under these conditions. Below I have produced a profit curve utilizing re-investment of capital and compounding.



The setup has not done as poorly in recent times, but it is still not a favorable one for the market.

Lastly, ignoring our Market Timing Course Price Action indicators, I examined how the market has performed during all "Worst 6 Months" of unfavorable Presidential Cycle years. Results are shown in the table below.

SPX Performance from the end of April through the end of October during unfavorable Presidential Cycle years.

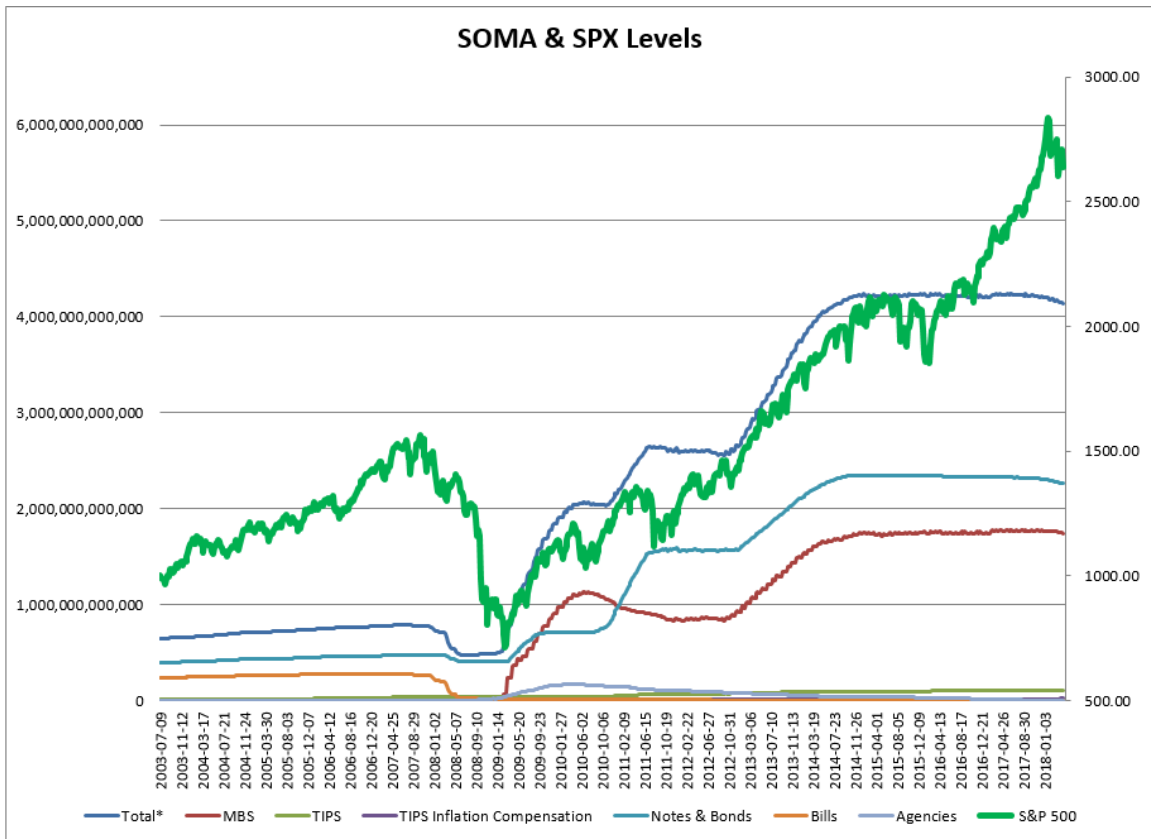
<u>Year</u>	<u>Return</u>	<u>Max Drawdown</u>	<u>High/Low Spread</u>
1961	5.07%	-1.38%	6.45%
1962	-13.37%	-21.28%	23.87%
1966	-11.93%	-20.62%	21.38%
1969	-6.34%	-15.09%	18.03%
1970	2.12%	-15.83%	23.47%
1974	-18.17%	-32.49%	36.31%
1977	-6.20%	-8.36%	12.56%
1978	-3.80%	-5.35%	16.92%
1981	-8.22%	-17.01%	19.16%
1982	14.84%	-12.22%	32.78%
1986	3.59%	-3.15%	11.09%
1989	9.92%	-1.79%	18.15%
1990	-8.10%	-10.96%	22.73%
1993	6.28%	-0.76%	7.77%
1994	4.75%	-2.45%	8.34%
1998	-1.18%	-16.77%	23.79%
2001	-15.18%	-24.38%	29.69%
2002	-17.75%	-28.36%	31.09%
2006	5.14%	-6.94%	12.93%
2009	18.72%	-0.76%	26.82%
2010	-0.29%	-14.77%	16.31%
2014	7.12%	-3.35%	10.53%
2017	<u>8.01%</u>	<u>-1.29%</u>	<u>9.44%</u>
<b>Avg</b>	<b>-1.09%</b>	<b>-11.54%</b>	<b>19.11%</b>

Eleven years finished higher and twelve lower for an average loss of just over 1%. But what was most interesting was the wild rides the market experienced during these 23 years. The average drawdown from the close of April entry point is -11.54%. And the last column is very eye-opening. This looks at the difference between the max run-up and the max drawdown over the 6 month period to see how wide of a range the SPX traded in. On average, the market saw a high-low range of 19.11% during the 6-month periods. That is exceptionally large. And only 4 of the 23 instances failed to see a range of at least 10%! If seasonal cycles have any say, the market could be in for a wild ride over the next 6 months.

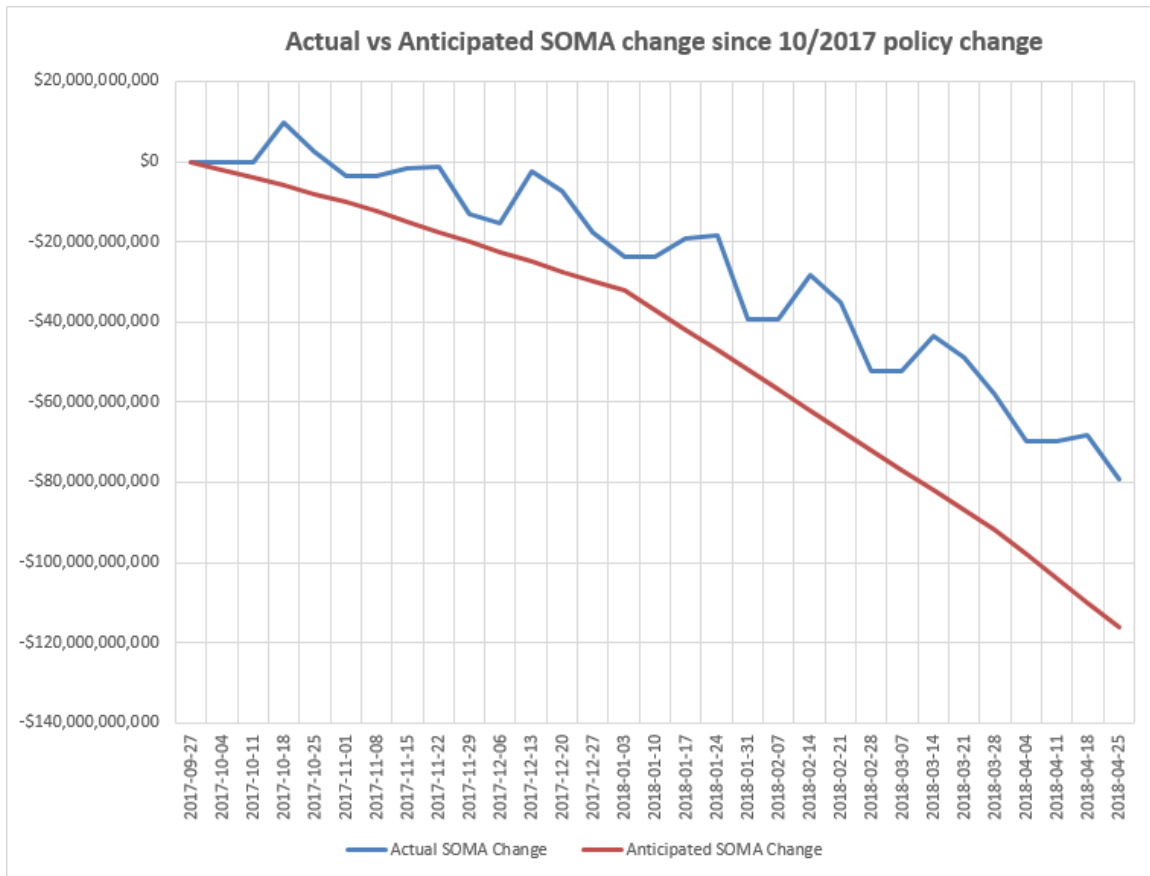
As I typically do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

*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) declined \$11.3 billion. We were expecting to see a sizable decline this past week, and we got it. The SPX fell 2.6% over the same period. This is not a big surprise, since the market has often struggled when there have been SOMA reductions. I also expect to see a sizable decline this week, though perhaps not as large as the last week. The current stated reduction rate is \$30 billion / month, and so far this month the SOMA is down about \$21 billion. Therefore, another \$9 billion would hit the mark on the dot – but hitting the mark exactly has not been the norm. I suspect we will fall a bit short of the stated \$30 billion. It will be difficult for the bulls to continue to post strong gains as liquidity winds continue to blow against them. We could get a bit of a reprieve in the early part of May. But the back half of the month should see more sizable SOMA reductions, or Quantitative Tightening (QT), which is the new term for it. And the gusts are set to increase further as QT is set to increase to \$40 billion / month starting in July and the \$50 billion / month beginning in October. Overall, I expect the current Fed policy will continue to act as a headwind for the bulls and leave the market more prone to liquidity events and sharp selloffs.

Bullish evidence is fading fast. We have 2 intermediate-term bullish studies from April on the Active List. They are both set to expire on Friday. The “Best 6 Months” ends on Monday. And the “Worst 6 Months” studies shown above indicate there could be some sizable downside volatility in the next several months. The Golden Cross is still hanging on, but that has not done well without support of any other Market Timing Course indicators. The Quantitative Tightening is a substantial bearish force, and remains a primary concern for me. Short-term evidence is still favorable for the bulls, and the market could see some gains this week, but by Friday, with most of the bullish evidence off the board, I anticipate turning outright bearish. I will keep my overall bias neutral for the next few days – meaning I am equally willing to take short-term trades in both longs and shorts. But without substantial new intermediate-term bullish evidence emerging this week, I’ll be much less inclined to trade long starting on Friday afternoon.

### **Catapult and Capitulative Breadth Statistics**

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

#### ***OpenCatapult 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.*

*[None tonight.](#)*

### Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
<b>BMV(1/3)</b>	<b>4/18/2018</b>	<b>\$52.35</b>	<b>\$52.33</b>	<b>-0.04%</b>		<b><i>sold on open</i></b>
<b>BMV(1/3)</b>	<b>4/19/2018</b>	<b>\$52.30</b>	<b>\$52.33</b>	<b>0.06%</b>		<b><i>sold on open</i></b>
<b>BMV(1/3)</b>	<b>4/20/2018</b>	<b>\$51.61</b>	<b>\$52.33</b>	<b>1.40%</b>		<b><i>sold on open</i></b>
<b>QQQ(1/4)</b>	<b>4/24/2018</b>	<b>\$161.50</b>	<b>\$164.35</b>	<b>1.76%</b>		<b><i>sold on open</i></b>
KHC(1/3)	4/25/2018	\$56.52	\$57.66	2.02%		<i>sell on open</i>
QCOM(1/3)	4/25/2018	\$49.94	\$51.11	2.34%		<i>sell on open</i>
QCOM(1/3)	4/26/2018	\$49.41	\$51.11	3.44%		<i>sell on open</i>

*KHC and QCOM both met their exit triggers and will be sold at the open on Monday.*

*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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