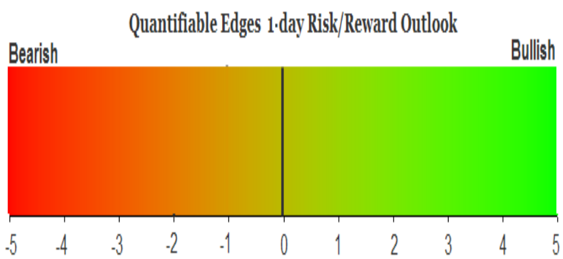
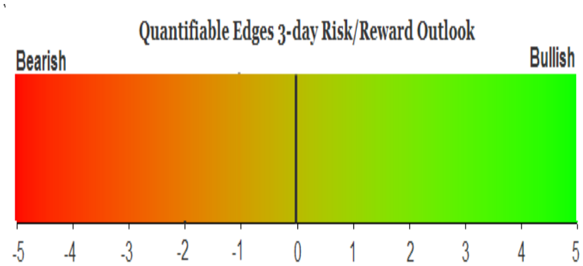
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 7, 2018 Volume 11 Issue 87

Market Overview





Signals Overview

Aggregator	CBI Reading
Flat	1

Tonight's Research Points

- Strong moves off short-term lows on Employment Days have been fairly rare but have so far hinted at a short-term downside edge.
- The NASDAQ has taken a leading position from the SPX.
- There was a large decline in the SOMA again last week. We expect this week to be much more moderate.

Short-term Outlook

The Bottom Line

Like the last couple of nights, the Aggregator is neutral and so am I.

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 4, 2018	SPY dip under 200ma but close above	1-2 days	Bearish			
May 2, 2018	SPX higher 1st day in May	1-4 days	Bearish			
Active - Long Term						
May 7, 2018	NASDAQ leading	int term	Bullish			
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

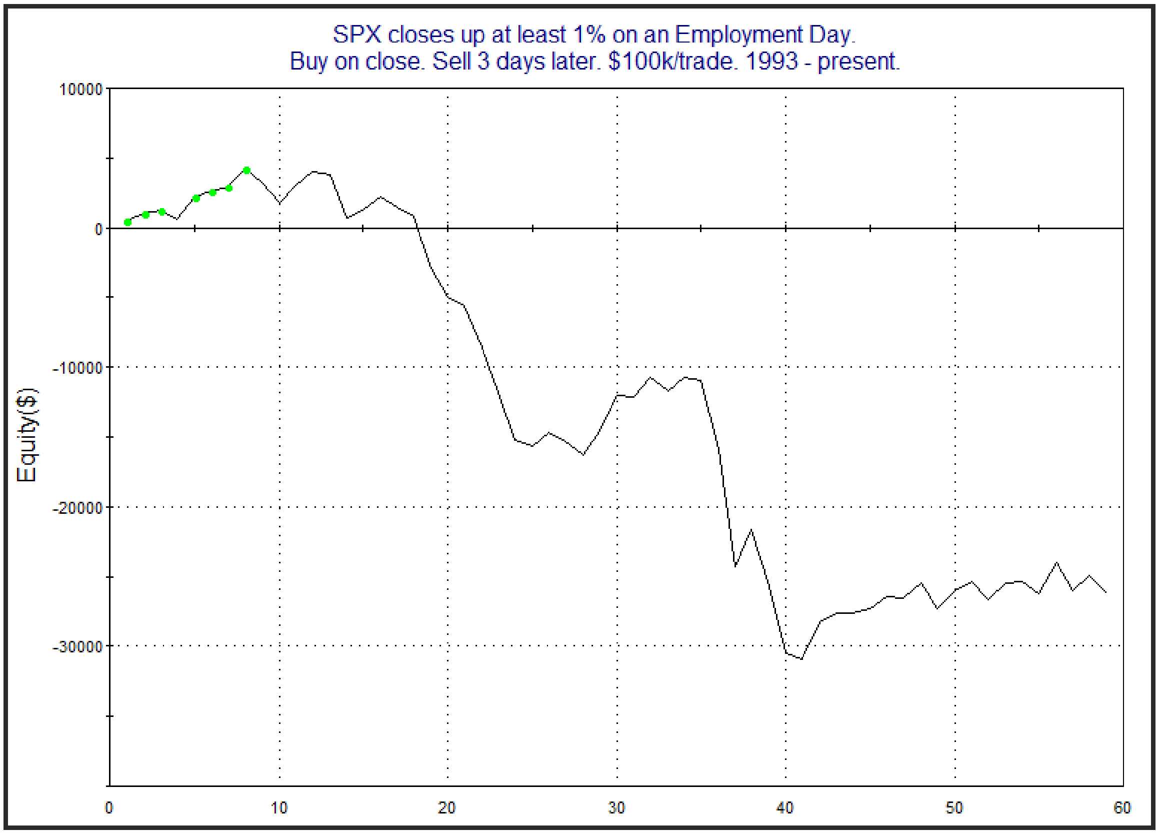
A down open reversed strongly and the market posted some big gains on the day. SPX closed up 1.3%, the NASDAQ rose 1.7% and the Russell 2000 rallied 1.2%. Breadth was positive as the NYSE Up Issues % was 74% and the Up Volume % came in at 82%. NYSE volume declined some from Thursday's level.

The bearish evidence I have seen the last few days was run over on Friday as the employment report and short-term oversold nature of the market combined for a sharp spike to the upside. Of course, as I noted Thursday evening, sharp moves on employment days have been the norm this year. But I thought it would be interesting to look at performance following Employment Days where the market rose substantially. The test below simply looks 1% or greater gains.

SPX closes up at least 1% on an Employment Day.
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	-37,390.80	59	27	32	45.76	1,438.23	4,090.16	-2,381.97	-10,421.45	0.60	0.51	-633.74
4	-22,958.94	59	28	31	47.46	1,176.01	3,165.57	-1,802.81	-4,929.60	0.65	0.59	-389.13
3	-26,263.84	59	28	31	47.46	1,096.31	2,718.52	-1,837.44	-8,419.83	0.60	0.54	-445.15
2	-16,052.00	59	28	31	47.46	809.19	1,819.17	-1,248.69	-4,765.60	0.65	0.59	-272.07
1	1,223.69	59	26	33	44.07	730.23	3,833.82	-538.26	-2,138.93	1.36	1.07	20.74

The numbers here look somewhat bearish. Unfortunately, the curves do not show a consistent edge. I have shown the 3-day curve below as an example.



Despite the negative numbers, the curve is not appealing for bears.

It is also notable that the market was short-term oversold prior to the rally. One test I ran that has somewhat interesting results looked at other times the setup triggered while rebounding from a 10-day low.

SPX closed at a 10-day low yesterday. Today is an employment day. SPX closes up at least 1% 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
5	-8,258.95	7	1	6	14.29	1,543.92	1,543.92	-1,633.81	-3,728.04	0.94	0.16	-1,179.85
4	-9,737.76	7	1	6	14.29	1,120.56	1,120.56	-1,809.72	-4,271.85	0.62	0.10	-1,391.11
3	-9,401.53	7	2	5	28.57	602.00	637.84	-2,121.11	-3,418.95	0.28	0.11	-1,343.08
2	-5,382.38	7	1	6	14.29	389.76	389.76	-962.02	-1,782.00	0.41	0.07	-768.91
1	-1,984.78	7	3	4	42.86	390.91	920.64	-789.38	-1,390.95	0.50	0.37	-283.54

Numbers here appear to have a strong bearish tilt. Of course, the low number of instances is a concern. Below is a list of all the instances with a 4-day holding period.

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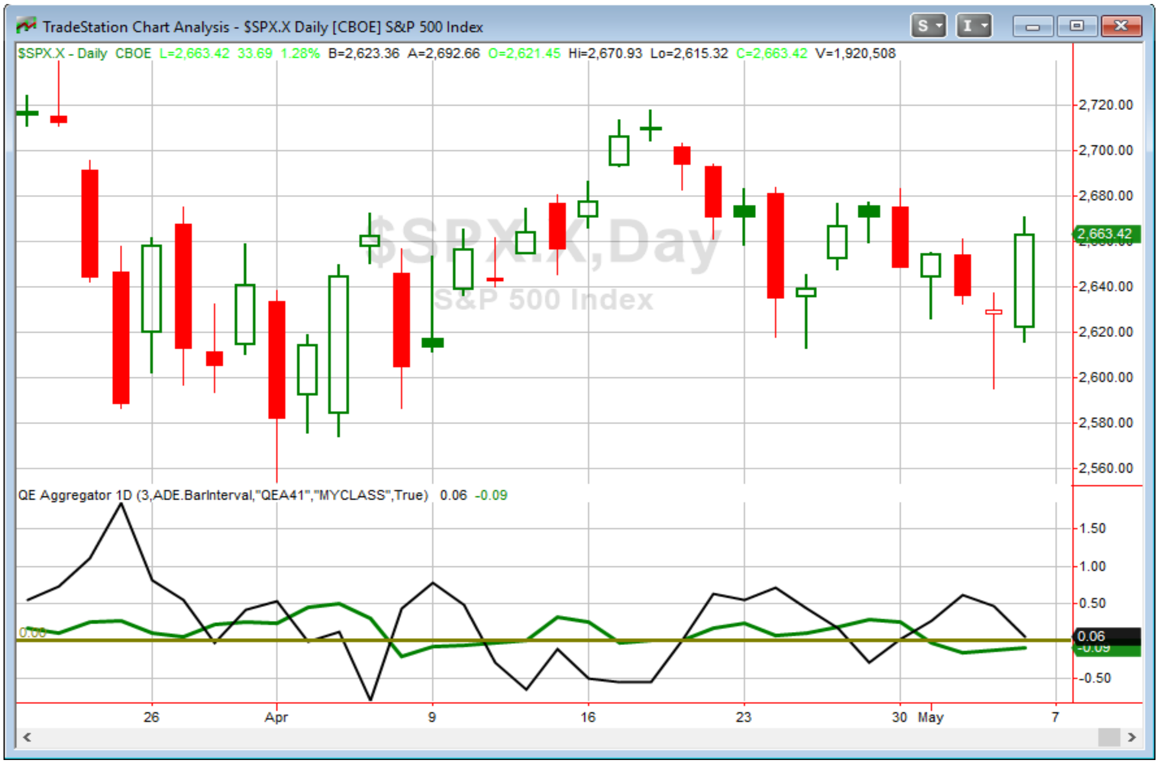
SPX closed at a 10-day low yesterday. Today is an employment day. SPX closes up at least 1% today. Buy on close. Sell 4 days later. $100k/trade. 1993 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
10/2/1998	Buy	$1,002.60	-4.30%	$608.85
10/8/1998	Sell	$959.45		($7,850.70)
12/4/1998	Buy	$1,176.74	-1.00%	$1,409.52
12/10/1998	Sell	$1,165.02		($1,092.00)
9/3/1999	Buy	$1,357.24	-0.41%	$302.95
9/10/1999	Sell	$1,351.66		($1,703.09)
5/5/2000	Buy	$1,432.63	-1.73%	$0.00
5/11/2000	Sell	$1,407.81		($3,966.81)
11/8/2013	Buy	$1,770.61	1.13%	$1,171.52
11/14/2013	Sell	$1,790.62		($558.32)
12/6/2013	Buy	$1,805.09	-1.64%	$353.65
12/12/2013	Sell	$1,775.50		($1,804.55)
12/4/2015	Buy	$2,091.69	-1.89%	$0.00
12/10/2015	Sell	$2,052.23		($2,592.52)

The selling has been consistent. There just are not enough instances to get me excited. Still, with the initial tendency appearing strong, I do believe this is worth tracking in the future. So while I will not include it on the Active List tonight, I will add it to the Quantifinder for future reference.

I have updated the Aggregator chart below.



Once again, the green Aggregator Line remained below zero. Negative readings mean net expectations from the Active List are for downside over the next few days. Meanwhile the black Differential Line held above 0. The positive Differential Line reading means SPX is oversold versus recent expectations. So expectations are negative but SPX is oversold. 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.

The remaining short-term studies are actually set to expire on Monday. With the intermediate-term neutral, that would also leave expectations flat. Of course, any new evidence that emerges based on Monday's action would change this. The Differential Pivot will be *inverted at* 2636.98 on Monday. That is 1.0% *below* Friday's close. An inverted pivot means that the Differential Line will cross through zero if SPX closes flat. In this case, SPX would need to close down at least 1.0% in order to remain oversold. Anything less than that and it will be considered overbought versus expectations as of Monday's close.

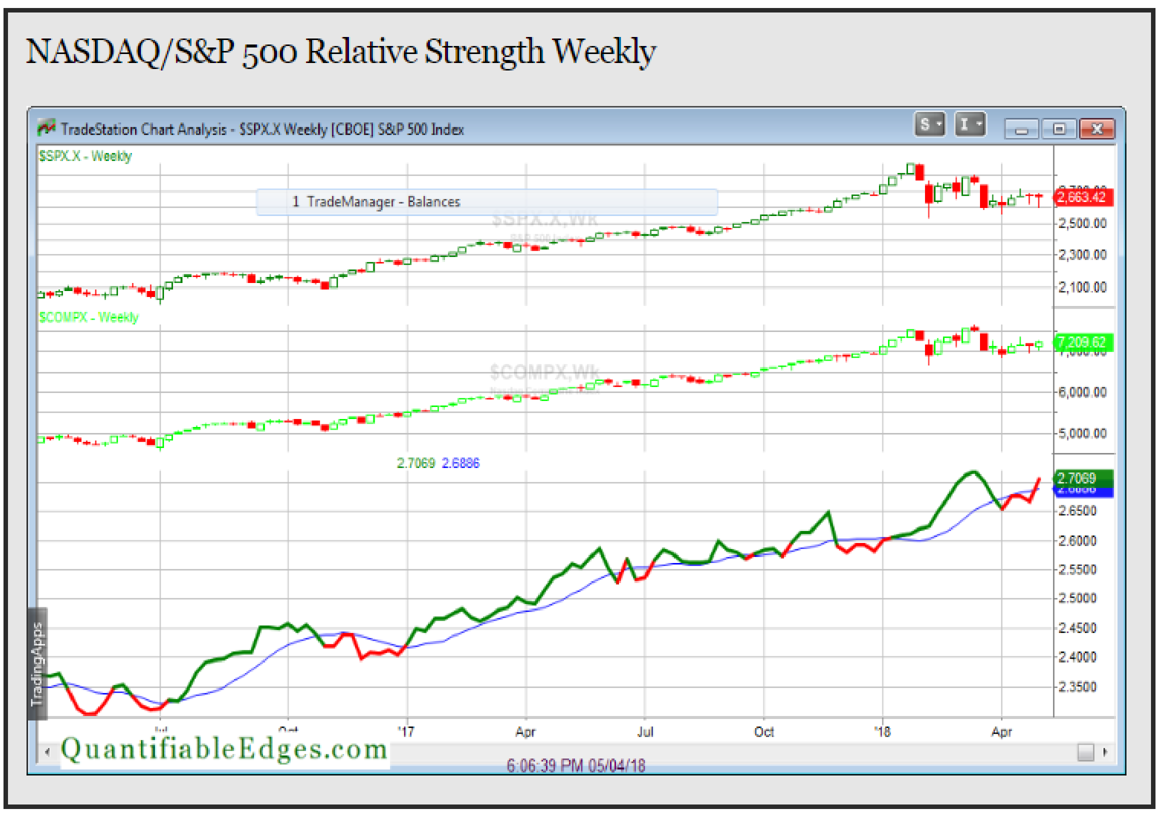
The combination of weak/expiring evidence and an inverted pivot is not one that is appealing when considering short-term index positions. There just is not a strong edge with favorable reward/risk right here. So I intend to wait until a more favorable setup emerges. That could be one day, or it could be many. When it happens, I'll be ready with funds available to trade.

Intermediate-term Outlook (2 weeks – 2 months) – ***updated 5/7– neutral***

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

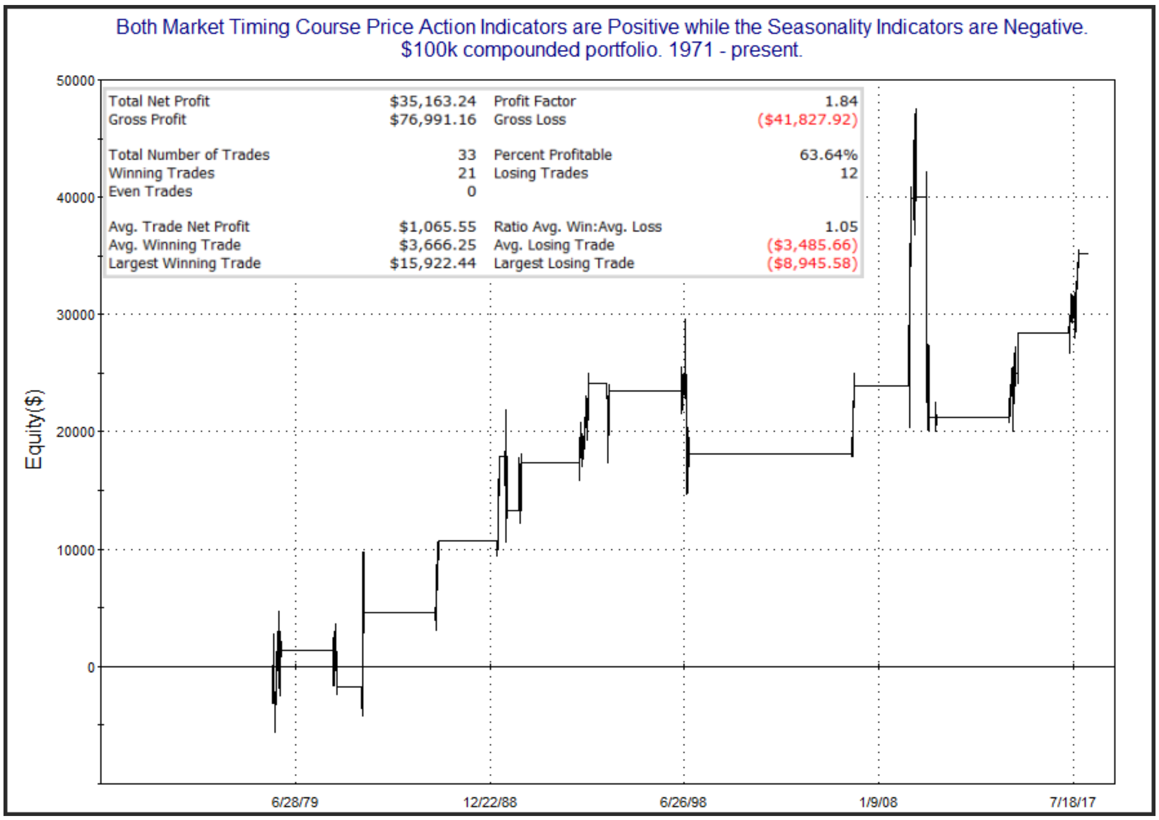
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the Quantifiable Edges Market Timing Course, which 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 there were no changes to the Combo Systems. *On Friday's close the NASDAQ moved into a leading position, which caused Combo Systems #1 and #2 to change to "long".*

The market finished mixed this past week. The SPX declined 0.2% while the NASDAQ gained 1.3%. The relative outperformance of the NASDAQ vs SPX helped it to retake a leading position based on our NASDAQ/SPX Relative Strength Indicator. This was after it spent 4 weeks in a lagging position. Below is a chart of the indicator from the website.



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, the market has performed substantially better when the NASDAQ has been leading. Over that time, the SPX has gained 1857.06 points when the NASDAQ has been leading versus 704.26 points when the NASDAQ has lagged. The difference for the NASDAQ has been even more dramatic, with the point gains being 5964.77 vs. just 1136.47. 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) unfavorable Presidential Cycle, and 4) "Worst" 6 months in effect. Below are updated stats showing SPX performance during this alignment.



We see here that similar formations have seen gains in the past. It is notable though that this chart has not made a whole lot of progress over the last 20 years. So perhaps the setup could be viewed as bullish, or perhaps your interpretation would be more neutral. In any case, it does not appear to be bearish. And as you can see near the top of this section, with both Market Timing Course price indicators still positive, two of the 3 "Combo" systems we track are now "Long".

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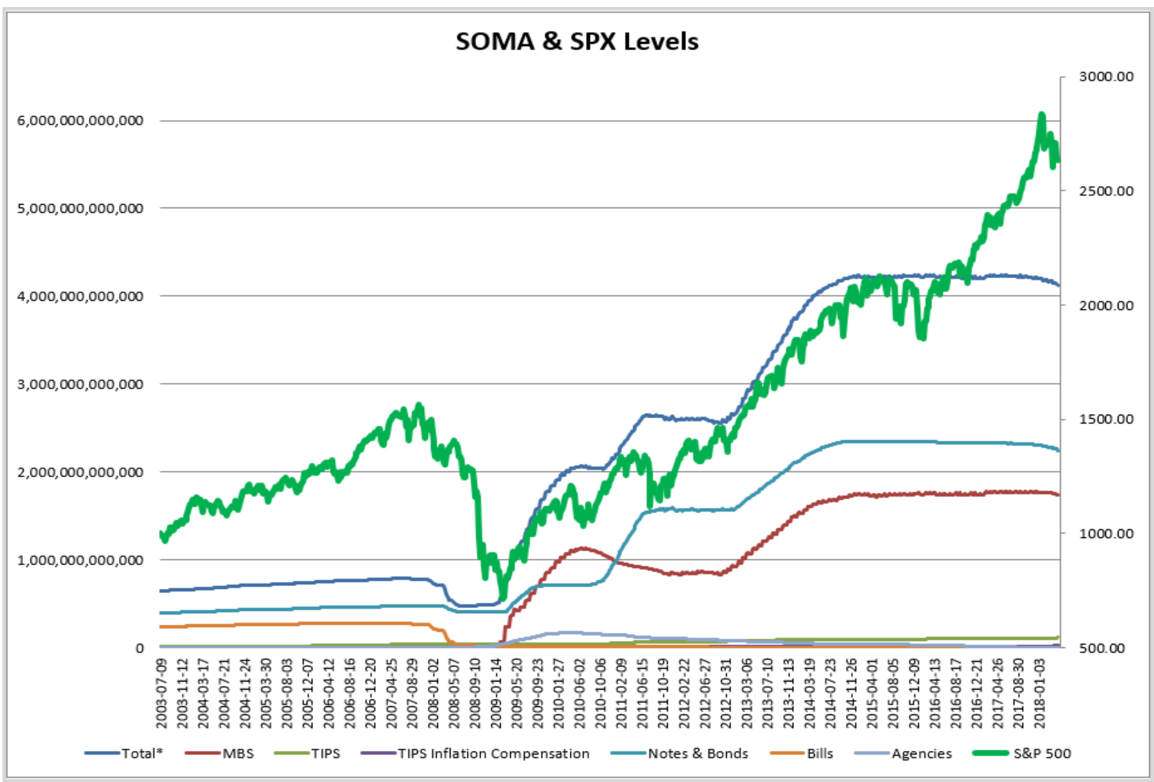
As I typically do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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.

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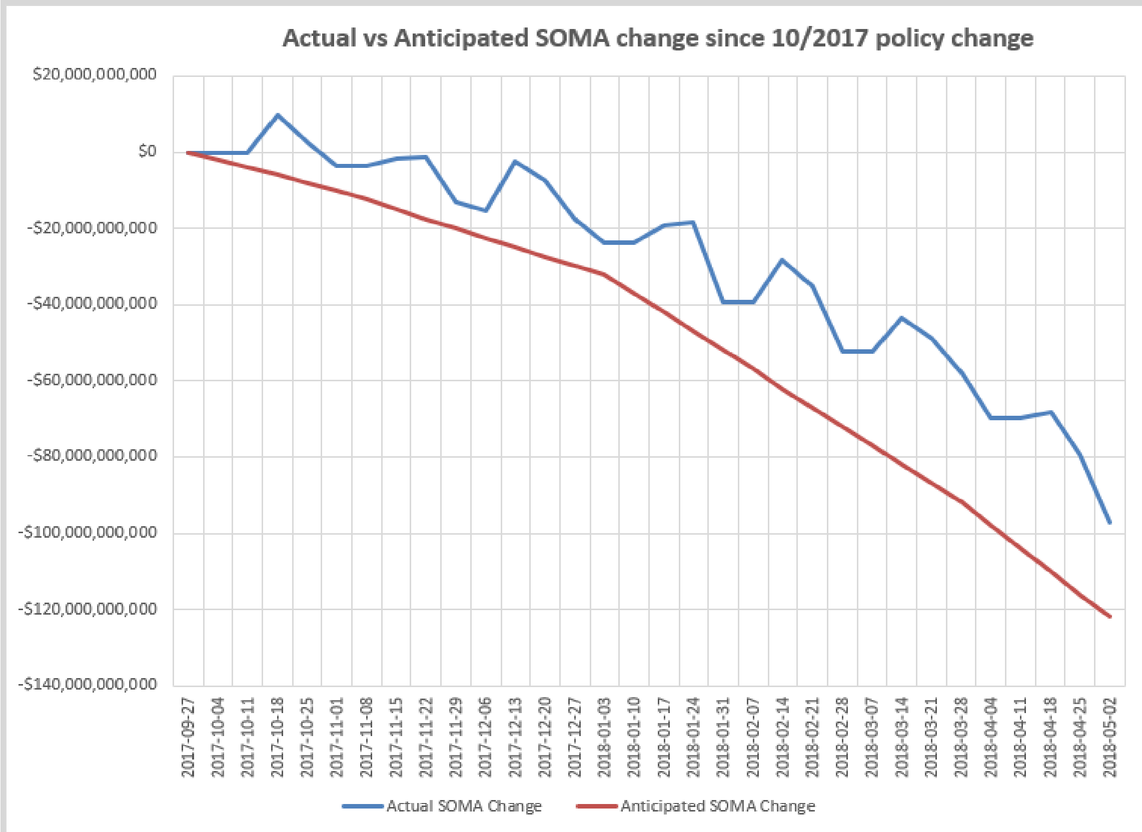
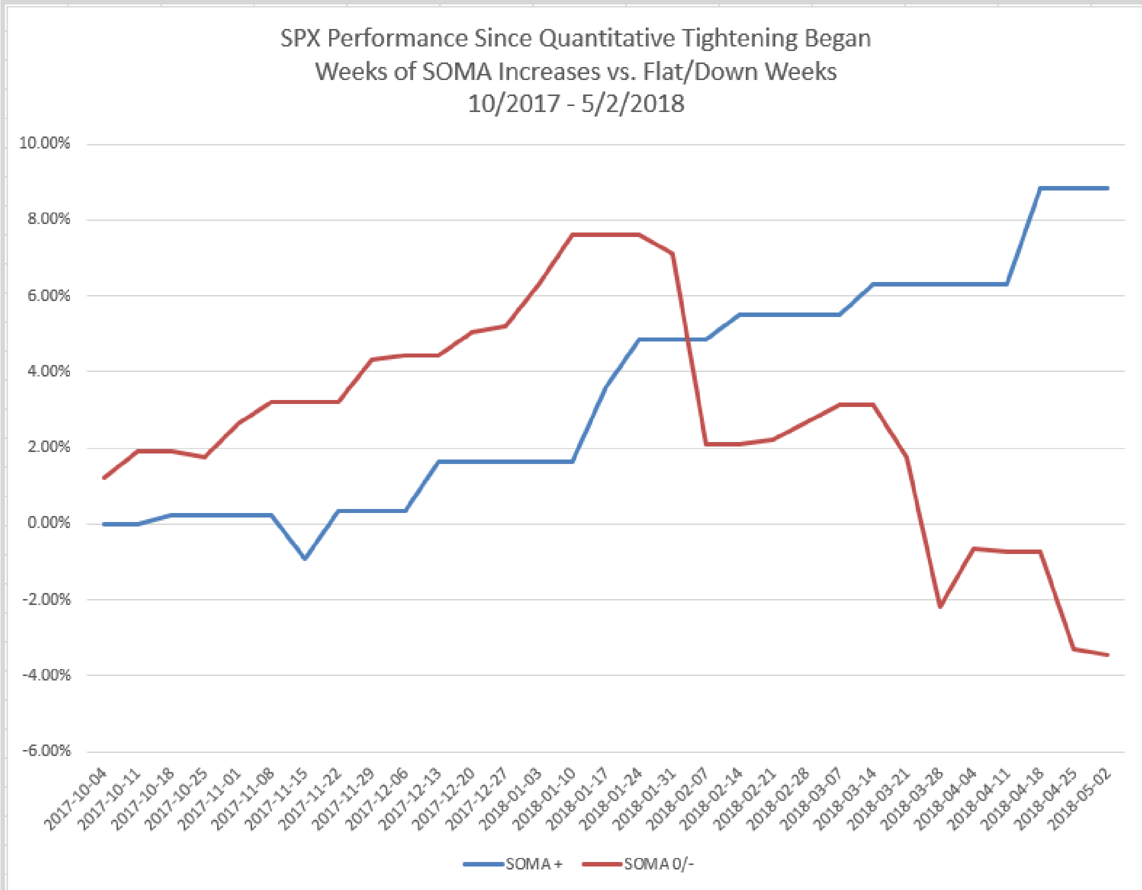


The Fed's SOMA this past week (Wednesday to Wednesday) declined $17.9 billion. We were expecting to see a sizable decline this past week, and we got it. The SPX fell 0.14% over the same period. A decline in the SPX is not a surprise, since the market has often struggled when there have been SOMA reductions. The chart below shows SPX performance since Quantitative Tightening (QT) began in October of 2017. It is broken down by weeks where the SOMA account rose at least 0.01% vs weeks where it came in flat or down.



It is plain to see that the damage has been done during those weeks in which the SOMA failed to expand. Of course, this is not unexpected for anyone that has followed the long-term chart above for any substantial period of time.

The next 2 weeks should see a bit of a reprieve for SOMA reductions based on the maturity schedule. This current week I expect to be fairly flat. And then next week we might even get a bit of a rise in the SOMA. Of course, that will also set up the 2nd half of the month for some sizable QT. Despite the possible short-term reprieve over the next couple of weeks, it will be difficult for the bulls to continue to post strong gains as liquidity winds continue to blow against them. And the gusts are set to increase further as QT is set to rise 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.

The NASDAQ outperformance changed my outlook a bit. I was set to turn to an outright bearish stance prior to that. But betting against a market with a leading NASDAQ and a Golden Cross formation has not been a good idea. Quantitative Tightening is a substantial bearish force, but for the next week and a half it may be a little less so. Rather than turning outright bearish, I will go with a neutral stance for now. That means I am willing to take

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short-term trade in either direction, though I will be a bit more conservative with entries for both longs and shorts. Should the NASDAQ begin to lag again, or other short-term bearish evidence emerge, then I could easily turn outright bearish. The market so far in 2018 has been quite volatile, and I expect that to continue for a while longer.

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

OpenCatapult Triggers

MDLZ @ $37.57 (buy @ limit)

Broad Market Large Cap CBI – 1(MDLZ)

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
MMM(1/3)	5/1/2018	$194.03	$199.36	2.75%		sell on open
MDLZ(1/3)	5/4/2018	$37.50	$38.90	3.73%		Catapult

MMM reached its exit trigger 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.