

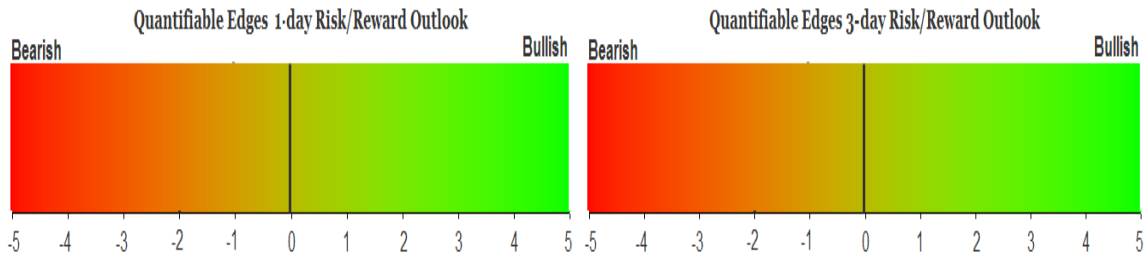
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

June 11, 2018

Volume 11 Issue 111

Market Overview



Signals Overview

Aggregator	CBI Reading
Flat	0

Tonight's Research Points

- The gap down and reversal to a 10-day high hinted at a pullback over the next couple of days.
- June opex week has been the weakest of any month.
- SOMA flows may provide a brief wind at the markets back for the next few days before again turning negative in the 2nd half of the month.

Short-term Outlook

The Bottom Line

The Aggregator is neutral, evidence is mixed and the market is neither strongly overbought nor oversold. So this does not appear to be a very compelling setup for bulls or bears.

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						
June 11, 2018	Gap up cls dn. Gap dn cls 10-hi & >200	1-2 days	Bearish			
June 7, 2018	VIX 10% above 10ma to 10% below	1-8 days	Bullish	2.10%	-1.20%	-2.55%
Active - Long Term						
June 7, 2018	SPX > 50-day Bollinger Band	1-50 days	Bullish	5.00%	-4.10%	-7.80%
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			

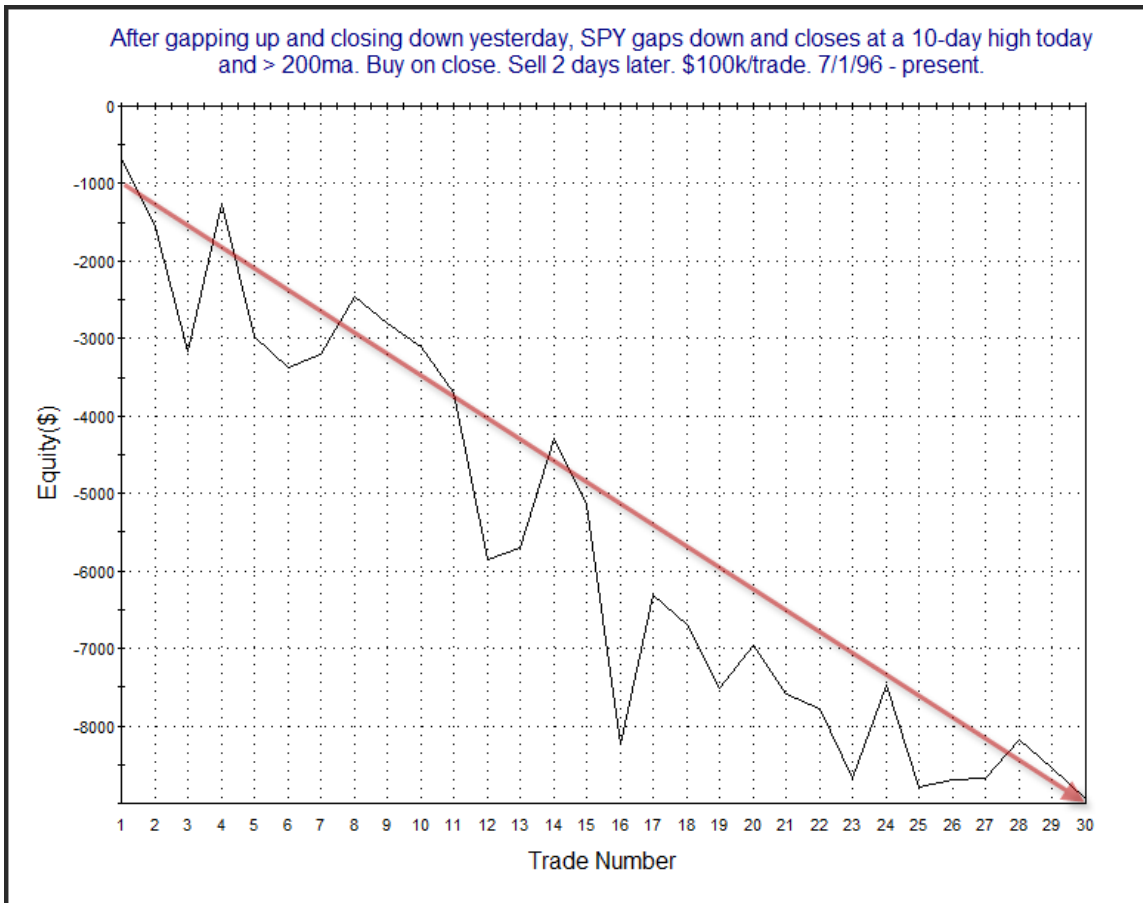
The Evidence

After a weak start, Friday put in an up day. The SPX rose 0.3%, the NASDAQ gained 0.1%, and the Russell 2000 climbed 0.3%. Breadth was positive as the NYSE Up Issues % was 58% and the Up Volume % came in at 68%. NYSE volume declined for the 2nd day in a row.

While SPY managing to recover from a gap down and closing at a new short-term high may seem like a positive, the study below saw Friday's "gap and reverse" as a potential negative. The study was last seen in the 5/22/15 Subscriber Letter. I have updated the results.

After gapping up and closing down yesterday, SPY gaps down and closes at a 10-day high today and > 200ma. Buy on close. Sell X days later. \$100k/trade. 7/1/96 - 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	-15,167.04	29	12	17	41.38	1,128.48	1,888.77	-1,688.75	-6,714.00	0.67	0.47	-523.00
4	-12,821.81	29	13	16	44.83	888.37	1,803.51	-1,523.16	-4,267.12	0.58	0.47	-442.13
3	-7,509.02	30	15	15	50.00	809.04	2,657.93	-1,309.64	-4,244.74	0.62	0.62	-250.30
2	-8,937.87	30	11	19	36.67	787.81	1,935.96	-926.52	-3,107.14	0.85	0.49	-297.93
1	-711.65	30	13	17	43.33	556.35	2,409.00	-467.31	-1,388.76	1.19	0.91	-23.72

The numbers here look somewhat bearish, with much of the damage being done by day 2. I also produced a profit curve assuming a 2-day holding period.



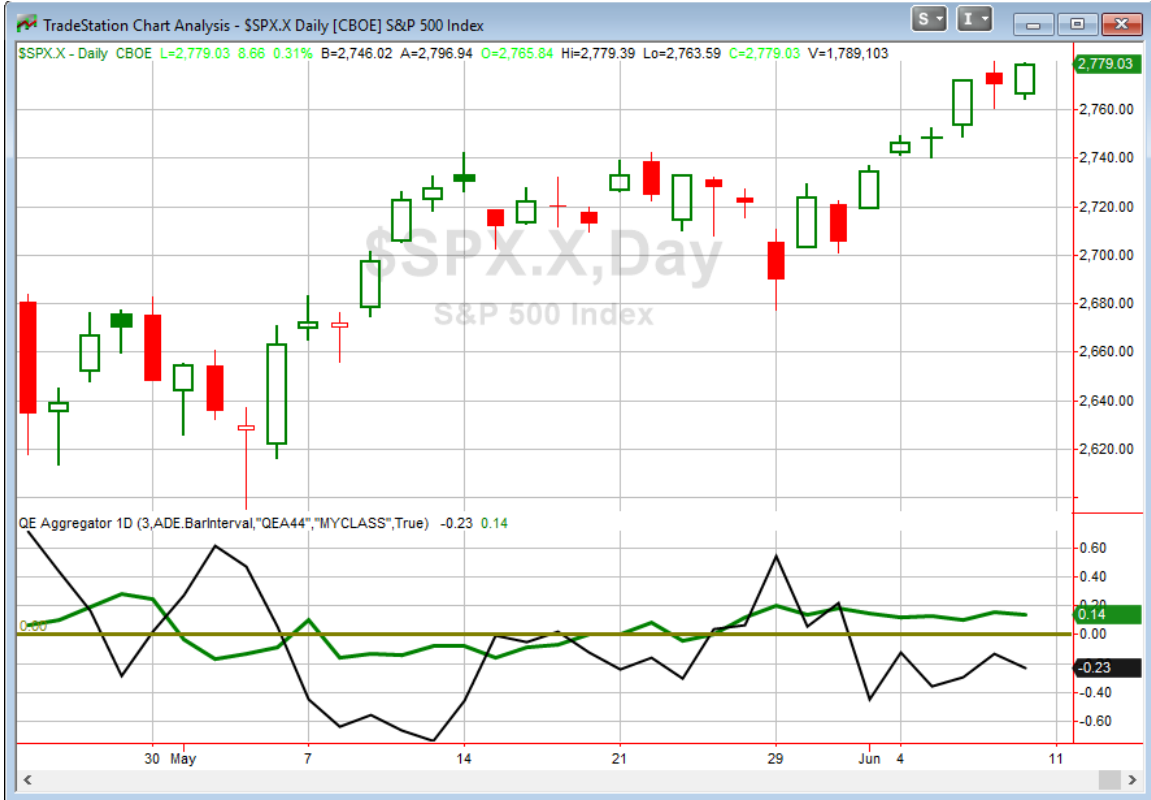
There is a bit of chop in this curve, but it is again making new lows and the overall slope seems good enough to warrant consideration. I included this study on the Short-Term Active List.

It is also somewhat notable that next week is opex week. Opex will often carry with it some bullish implications. But June since 1984 when S&P options began trading, June has been the weakest opex of any month. This can be seen in the table below, which I lifted from the 3/12/18 subscriber letter (not updated).

OpEx week SPX performance by month. \$100k/trade. 1984 - present. (Excludes September 2001)												
Month	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
12	29,033.77	34	26	8	76.47	1,458.03	5,868.16	-1,109.38	-4,176.33	1.31	4.27	853.93
11	5,787.67	34	21	13	61.76	1,418.95	3,718.25	-1,846.95	-8,351.64	0.77	1.24	170.23
10	26,245.77	34	25	9	73.53	2,142.44	7,282.10	-3,035.03	-9,109.98	0.71	1.96	771.93
9	15,176.65	33	21	12	63.64	1,523.50	5,313.08	-1,401.40	-4,975.04	1.09	1.90	459.90
8	-1,954.26	34	18	16	52.94	1,432.07	4,329.72	-1,733.21	-5,670.55	0.83	0.93	-57.48
7	1,522.27	34	18	15	52.94	1,418.70	6,921.25	-1,600.96	-7,953.12	0.89	1.06	44.77
6	-1,985.79	34	19	15	55.88	1,172.43	3,786.09	-1,617.47	-3,998.19	0.72	0.92	-58.41
5	2,345.79	34	17	17	50.00	1,821.90	4,850.40	-1,683.91	-4,959.45	1.08	1.08	68.99
4	30,132.39	34	22	12	64.71	2,194.65	5,731.96	-1,512.48	-3,580.15	1.45	2.66	886.25
3	30,457.88	34	24	10	70.59	1,933.52	7,515.60	-1,594.66	-6,711.66	1.21	2.91	895.82
2	16,205.42	35	21	14	60.00	1,605.48	4,281.46	-1,250.70	-6,814.80	1.28	1.93	463.01
1	5,478.21	35	16	19	45.71	2,094.03	5,389.00	-1,475.07	-5,383.93	1.42	1.20	156.52

So June cannot be counted on for bullish opex seasonality. In fact, we won't see strong bullish opex seasonality again until October.

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



Even with tonight’s bearish evidence, 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.

With the current studies on the Active List, expectations are slated to remain bullish on Monday. This could change if more bearish evidence emerges. The Differential Pivot will be *slightly inverted at 2782.20* on Monday. That is 0.1% *above* Friday’s close. An inverted pivot means that the Differential Line will cross through zero if SPX closes flat. In this case, SPX will need to rise over 0.1% in order to remain overbought. Otherwise, it will be considered “oversold” versus expectations as of Monday’s close.

Evidence is mixed. The Aggregator is neutral. And with the slightly inverted Differential Pivot, SPX could easily finish overbought or oversold on Monday. In other words, there is a good amount of doubt and contradiction. At some point – likely soon – we will get a compelling buildup of evidence and a favorable reward/risk setup. But we are not there right now, so I will continue to wait until a better setup emerges.

Intermediate-term Outlook (2 weeks – 2 months) – updated 6/11– neutral

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

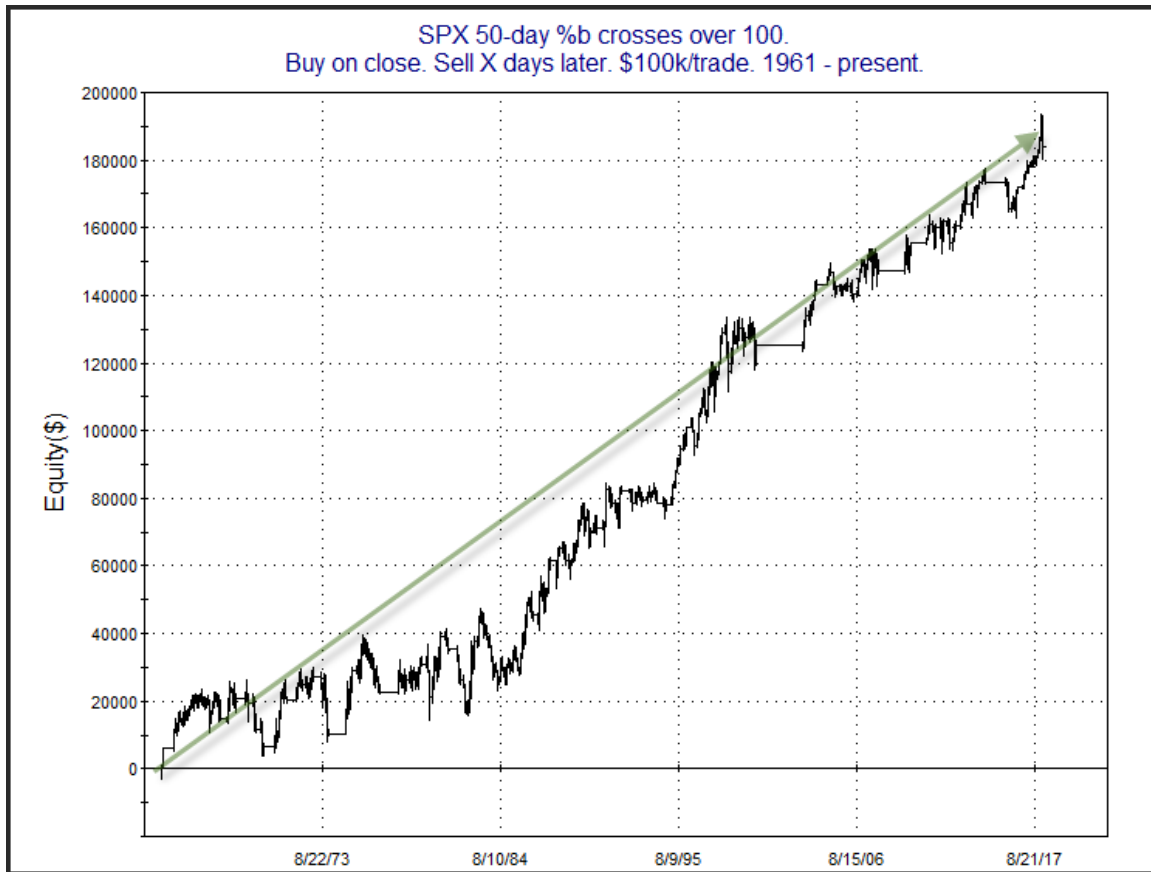
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#), 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. *There were no changes to the Combo Systems this week as #1 remained “flat” and #2 and #3 remained “long”.*

The market put in strong gains this past week. The SPX rose 1.6% while the NASDAQ gained 1.2%. Both the NASDAQ and the Russell 2000 closed at all-time highs on Wednesday. There was one new intermediate-term study that emerged which I discussed in Wednesday night’s letter. I have copied it below.

One study from the 9/19/17 Subscriber Letter that triggered today has some potential intermediate-term implications, and it is fairly interesting, so I figured I would talk a little about it. This study looked at the SPX closing price in relation to its 50-day Bollinger Bands. In it I used 2 standard deviations in the Bollinger Band calculation. I used %b to measure where we fell. For those unaware, %b simply measures the distance between the 2 bands. So a reading of 0 means price is right at the lower band. A reading of 100 is right at the upper band. A reading of 50 would be right at the moving average being used – in this case the 50ma. So a move 2 standard deviations above the 50ma would be a %b reading of 100. An updated results table for this study is below.

SPX 50-day %b crosses over 100. Buy on close. Sell X days later. \$100k/trade. 1961 - 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
50	183,782.88	134	81	53	60.45	4,890.91	18,408.18	-4,007.18	-15,795.00	1.22	1.87	1,371.51
45	154,783.22	140	80	60	57.14	5,041.78	15,816.57	-4,142.66	-25,812.76	1.22	1.62	1,105.59
40	166,270.44	145	87	58	60.00	4,520.09	17,624.67	-3,913.41	-15,540.70	1.16	1.73	1,146.69
35	143,843.63	153	92	61	60.13	4,043.78	15,782.13	-3,740.72	-13,617.00	1.08	1.63	940.15
30	98,549.69	159	94	65	59.12	3,364.92	11,920.74	-3,350.05	-10,485.00	1.00	1.45	619.81
25	65,401.52	167	95	72	56.89	3,047.45	10,859.94	-3,112.59	-8,732.16	0.98	1.29	391.63
20	60,977.97	178	102	76	57.30	2,654.30	9,501.30	-2,760.00	-10,205.38	0.96	1.29	342.57
15	67,130.23	195	114	81	58.46	2,326.50	7,843.46	-2,445.57	-9,763.44	0.95	1.34	344.26
10	49,765.27	218	137	81	62.84	1,683.79	8,239.16	-2,233.50	-9,133.53	0.75	1.28	228.28
5	26,181.30	265	152	113	57.36	1,129.57	5,030.81	-1,287.73	-5,817.77	0.88	1.18	98.80

Results generally appear moderately bullish. They seem to suggest that the kind of strong momentum that would have SPX closing above its 50-day Bollinger Band favors more upside over a possible reversal. The “% Profitable” is not terribly high, but I produced a profit curve below to see how the edge has played out over time.

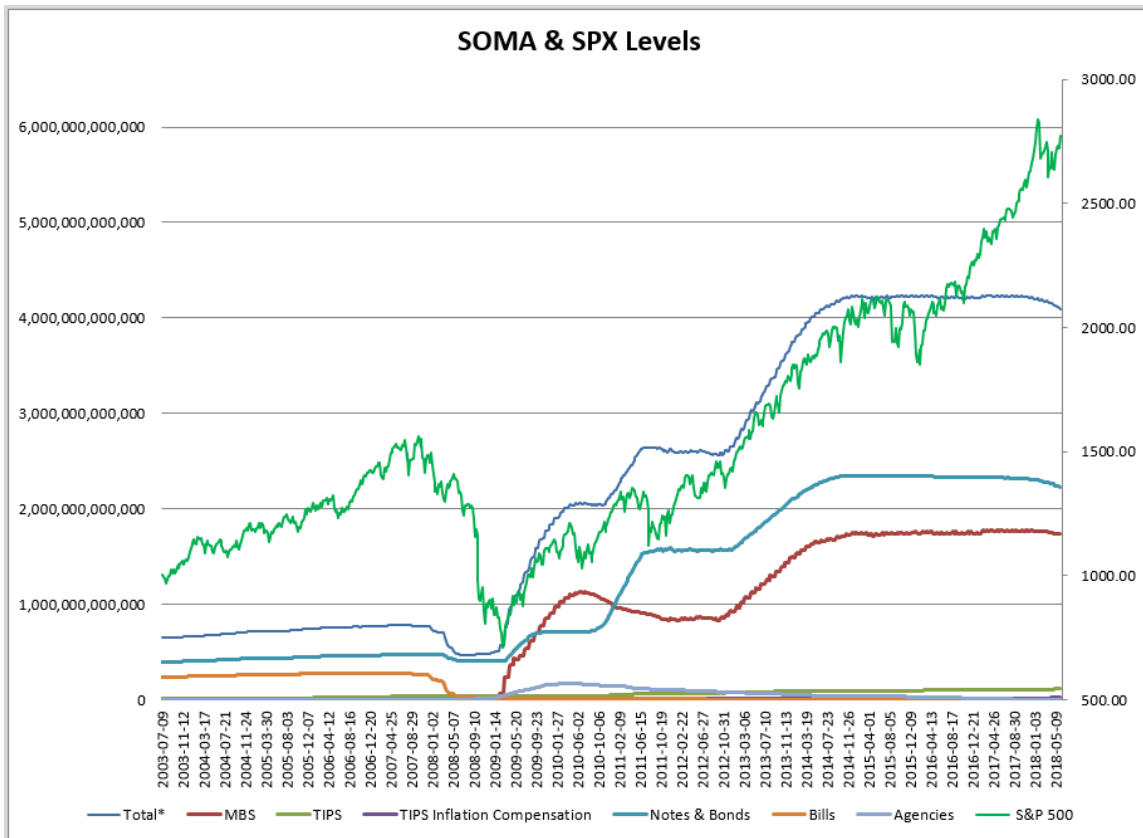


That's a pretty steady upslope for a study without a very high "% Profitable". Overall, I like this study enough to add it to the intermediate-term active list.

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.

In October 2017 the Fed began reducing the size of the SOMA by not reinvesting some maturities in MBS and treasuries. That program is expected to continue for the next few years. Below are long and short-term views of SOMA and SPX. First, the long-term view (back to 2003).



The table below is from the Fed's website and shows the changes this past week.

« As of 05/30/2018

SECURITIES HOLDINGS AS OF
June 6, 2018

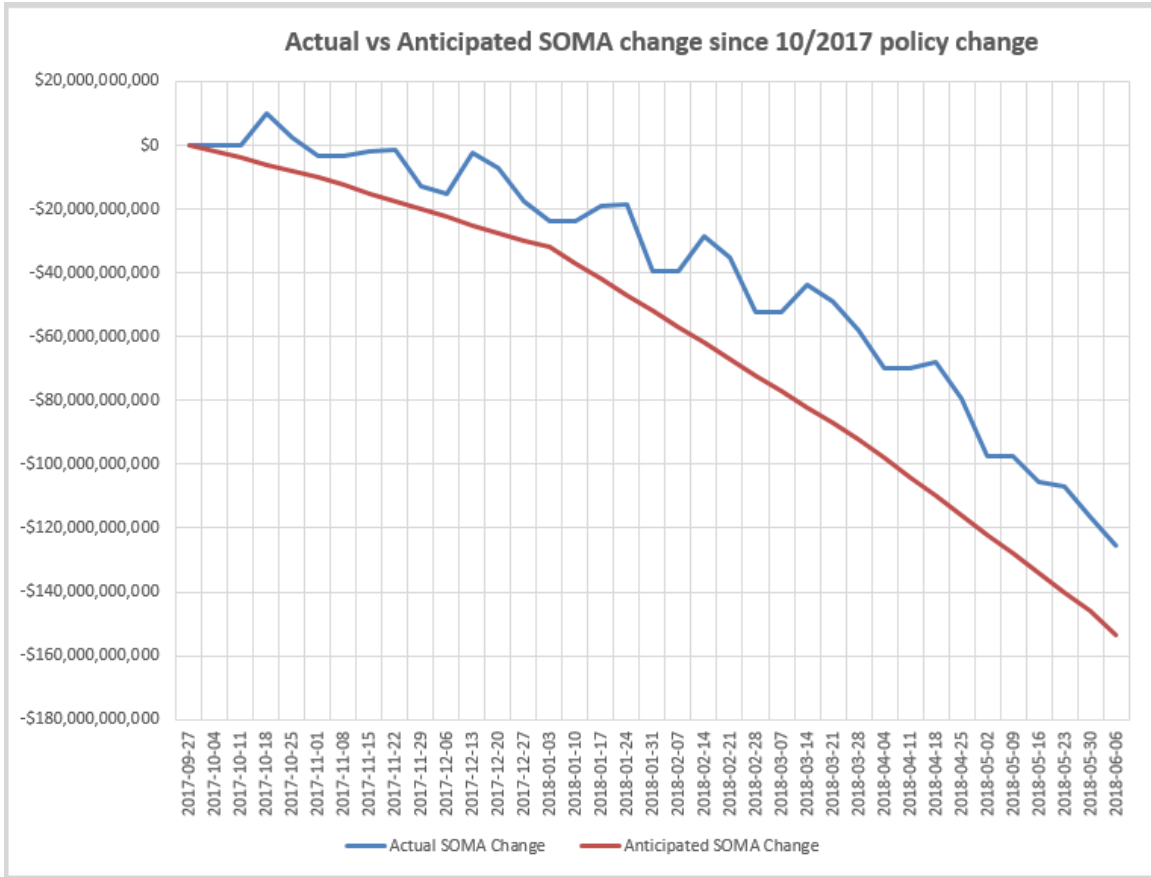
Security Type	Total (in Thousands)
US Treasury Bills (T-Bills)	
US Treasury Notes and Bonds (Notes/Bonds)	2,224,344,406.1
US Treasury Floating Rate Notes (FRN)	17,816,385.9
US Treasury Inflation-Protected Securities (TIPS)*	114,860,063.8
Federal Agency Securities**	4,391,000.0
Agency Mortgage-Backed Securities***	1,734,592,848.9
Total SOMA Holdings	4,096,004,704.7
Change From Prior Week	-9,365,319.9

*Does not reflect inflation compensation of 20,851,352.6

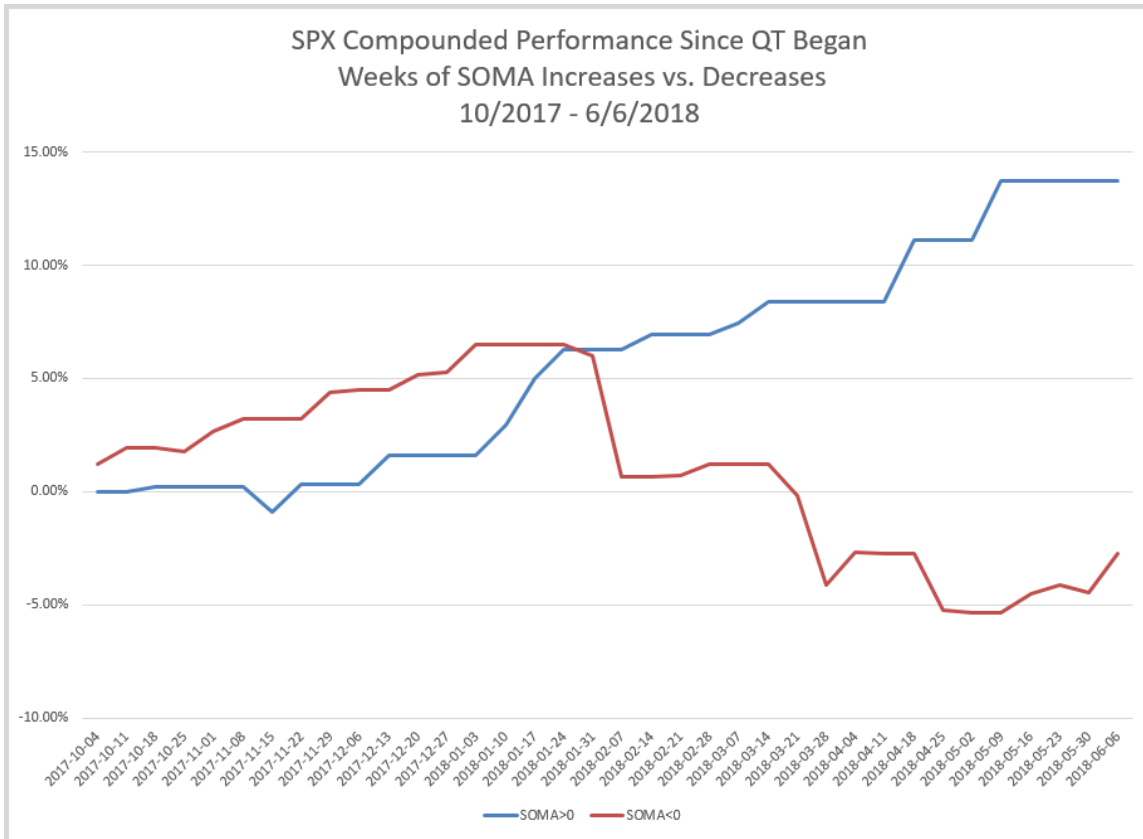
**Fannie Mae, Freddie Mac and Federal Home Loan Bank

***Guaranteed by Fannie Mae, Freddie Mac, and Ginnie Mae. Current face value of the securities, which is the remaining principal balance of the securities.

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



The Fed’s SOMA this past week (Wednesday to Wednesday) saw a decline of \$9.4 billion. The drop was all due to expiring treasuries, as some other SOMA securities (including AMBS) saw mild increases. The “Actual vs Anticipated” chart simply shows that this is a somewhat steep overall decline when the monthly reduction is about \$30 billion/month. Despite the SOMA reduction, the SPX posted a sizable gain of 1.77%. That is the largest % gain for SPX during a SOMA contraction week since 4/26/17, over a year ago. More typically, the market has struggled during SOMA contraction weeks, and flourished when the SOMA has seen expansions. I discuss this in detail in the Fed-Based Quantifiable Edges for Stock Market Trading Research Paper. This next chart shows compounded results since Quantitative Tightening (QT) began in October 2017 of being long SPX during SOMA expansion weeks vs SOMA contraction weeks. It is updated from last week.



Expansion weeks have been positive on a fairly consistent basis. Reduction weeks have been choppy and net losers, even with the strong move up this past week. So what is ahead for this upcoming week, ending 6/13? As you can see in the table below, there are no treasury expirations set until the 30th. So any reductions between now and then will be in the AMBS securities. Those are a bit harder to anticipate the timing of, since there is a settlement lag, and the amount varies depending on prepayments. In looking at recent past months, weeks that ended either on the 13th or 14th actually saw mild increases in the size of the SOMA. This occurred in March, April, and December. So we could see a small bump in the SOMA this week. The next week, ending on the 20th, appears likely to undergo a small decline.

« As of 05/30/2018		SECURITIES HOLDINGS AS OF				
		June 6, 2018				
Summary		T-Bills	T-Notes and T-Bonds	FRN	TIPS	Agencies
Maturity Date	CUSIP	Coupon (%)	Par Value (in Thousands)	% of Total Outstanding ¹	Change in Par from Prior Week ²	Change in Par from Prior Year ²
6/30/18	912828R93	0.625	3,792,895.4	12.73%		
6/30/18	912828VK3	1.375	10,861,000.0	31.03%		
6/30/18	912828QT0	2.375	15,799,639.4	52.78%		
7/31/18	912828S68	0.750	1,815,682.0	6.53%		
7/31/18	912828VQ0	1.375	6,270,000.0	17.91%		
7/31/18	912828QY9	2.250	20,376,532.0	68.23%		

Overall, Fed policy should continue to act as a headwind in the weeks to come. And that headwind will increase from \$30 billion/month to \$40 billion/month starting in July.

My overall outlook is little changed this week. The SPX stretching beyond its 50-day Bollinger Band appears to be a favorable sign. And the continued NASDAQ outperformance along with SPX Golden Cross formation has led to solid gains in the past. So those are some things the bulls can point to. But Quantitative Tightening is a substantial bearish force, and long-term seasonal cycles like the “Best 6 Months” and the Presidential Cycle are currently unfavorable. I am keeping my outlook neutral. That means I am willing to take short-term trades in either direction, though I will be a bit more conservative with entries for both longs and shorts. After a volatile start to the year, the market has put in some solid gains in recent weeks. I still believe there could be some volatility this summer, as the shrinking SOMA leaves the market more prone to liquidity events, and the negative seasonality also leaves the door open for the bears. I will continue to monitor the market closely in search of new and compelling evidence. But right now I am wary of betting too aggressively in either direction.

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
EWZ	5/30/2018	\$35.33	\$34.14	-3.37%		Sell on close > \$35.01

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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