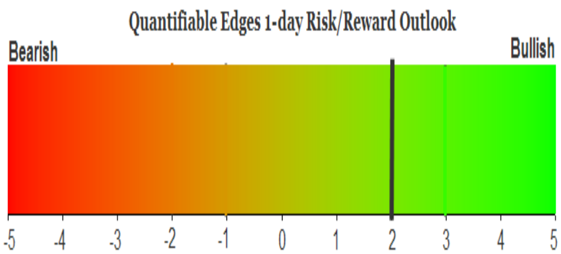
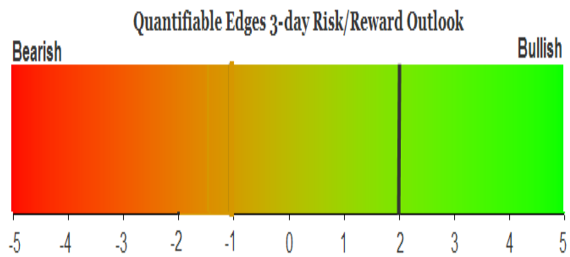
# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 19, 2018 Volume 11 Issue 224


## Market Overview




## Signals Overview

| Aggregator | CBI Reading |
|---|---|
| Long | 4 |

### *Tonight's Research Points*

- Thanksgiving Week has been seasonally bullish.
- Quantitative Tightening (QT) should come in high

***Short-term Outlook***
***The Bottom Line***
The studies are still pointing bullish. SPX is not yet overbought, but it will be unless it closes down a fair amount on Monday. Reward/risk seems to slightly favor the bulls.

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***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 | | | | | | |
| November 16, 2018 | Gap dn, 10-low, reverse up. Close<200 | 1-3 days | Bearish | | | |
| November 14, 2018 | Down 4 days. No turn on Tuesday | 1-6 days | Bullish | 2.30% | -1.30% | -2.70% |
| November 13, 2018 | Unfilled gap down 2x < 200ma | 1-5 days | Bullish | | | |
| November 13, 2018 | Down 3. Turnaround Tuesday | 1-5 days | Bullish | | | |
| Active - Long Term | | | | | | |
| November 8, 2018 | FTD with strong breadth & 20-day high | int term | Bullish | | | |
| November 1, 2018 | Best 6 Month During Pres Yr 3 | 1-6 months | Bullish | 17.70% | -3.10% | -7.20% |
| October 25, 2018 | CBI 10+. SPX 50-day low | 1-20 days | Bullish | 7.40% | -4.30% | -8.40% |
| October 1, 2018 | Quantitative Tightening $50billion/mo | 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***

Friday was a day of mixed results. The SPX closed up 0.2%, the NASDAQ lost 0.2%, and the Russell 2000 rose 0.2%. Breadth was positive as the NYSE Up Issues % was 53.1% and the Up Volume % came in at 52.9%. NYSE volume rose as it typically does on opex Friday.

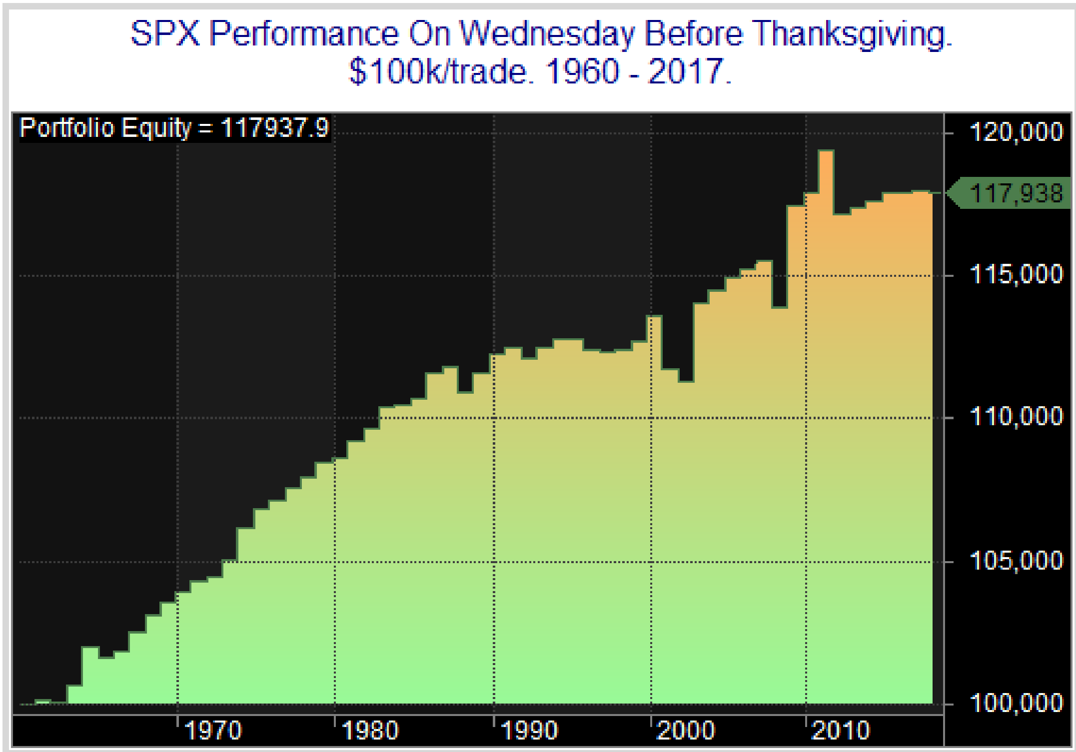
The mild action did nothing to trigger compelling price-action based studies. But Thanksgiving week has shown some strong seasonal tendencies over the years. This is something I last showed in the 11/20/17 subscriber letter. I have re-run those studies and updated them below. (Note, due to a current bug in Tradestation that is not running studies back to the 60s correctly, I recreated these studies in AmiBroker. So the format looks a bit different.)

This first one breaks down performance during Thanksgiving week by day.

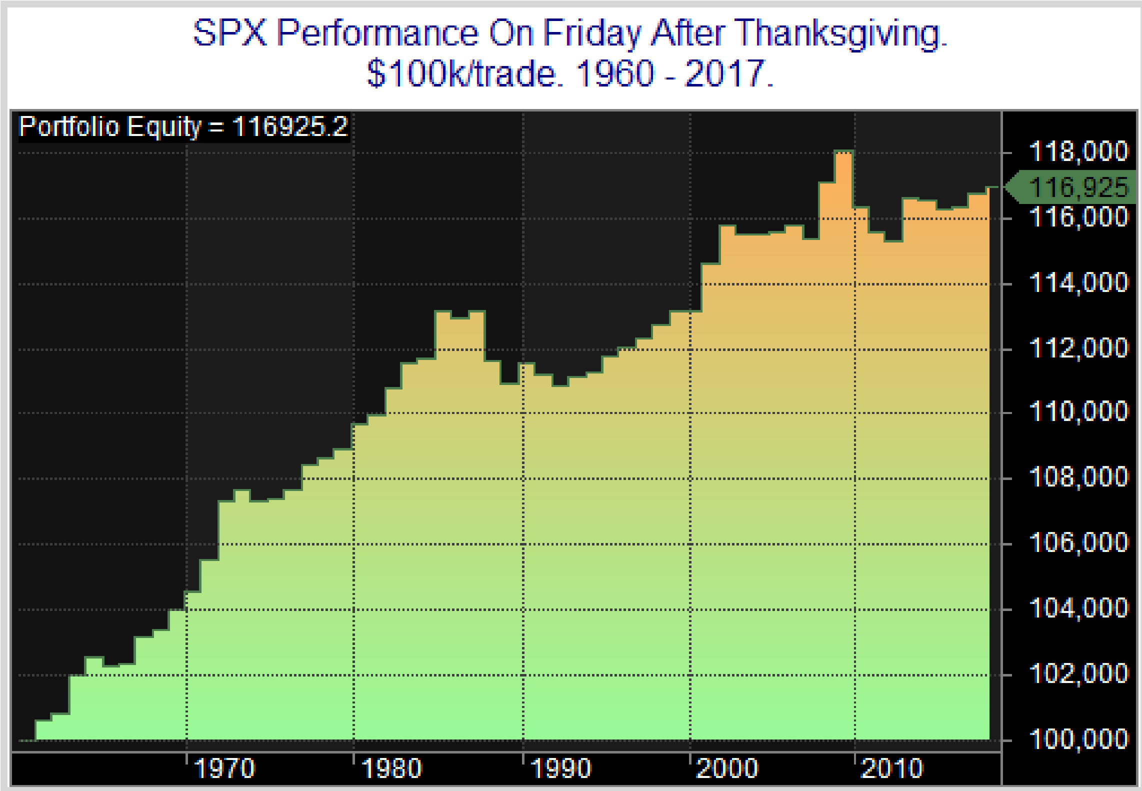
Thanksgiving Week Performance Broken Down by Day of Week.
$100k/trade in SPX. 1960 - 2017.

| Day | Net Profit | # Trades | # of winners | # of losers | % of Winners | W. Avg. Profit | L. Avg. Loss | Avg Profit/Loss | Profit Factor |
|---|---|---|---|---|---|---|---|---|---|
| Monday After | -21221.34 | 58 | 20 | 38 | 34.48 | 912.63 | -1038.79 | -365.89 | 0.46 |
| Friday | 16925.18 | 58 | 42 | 16 | 72.41 | 580.47 | -465.91 | 291.81 | 3.27 |
| Wednesday | 17937.86 | 58 | 45 | 13 | 77.59 | 586.59 | -650.69 | 309.27 | 3.12 |
| Tuesday | 3153.02 | 58 | 35 | 23 | 60.34 | 559.75 | -714.7 | 54.36 | 1.19 |
| Monday | 3512.35 | 58 | 27 | 31 | 46.55 | 1033.98 | -787.27 | 60.56 | 1.14 |

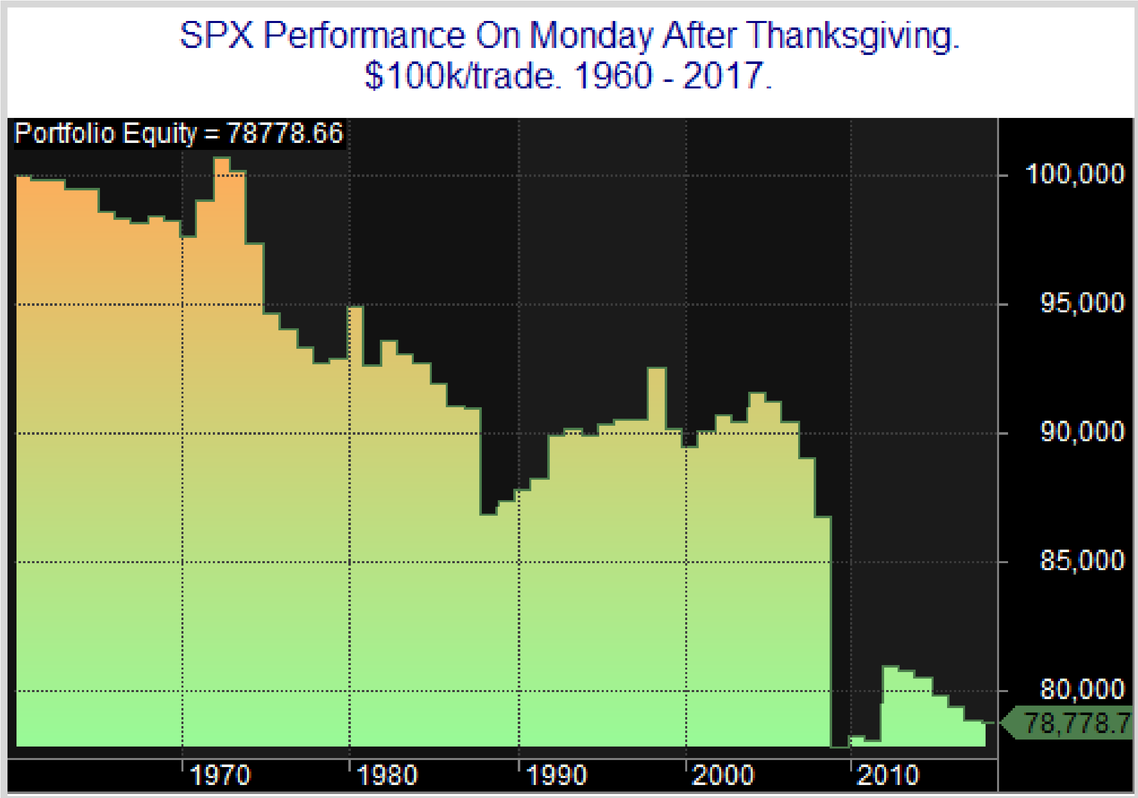
Monday and Tuesday don't show anything suggesting an edge. Wednesday and Friday, on the other hand, appear to be strongly bullish. And the Monday after Thanksgiving appears to exhibit a possible bearish edge. But before we jump to conclusions, let's examine the profit curves for Wednesday, Friday, and the following Monday. First below is Wednesday.




This curve looks to be strong. While there were a few bad Wednesdays, they were overwhelmed by the good ones. The next chart looks at Fridays after Thanksgiving.




This curve doesn't appear quite as strong as the Wednesday curve. Still, the general upslope still appears to be intact. To me it appears both Wednesday and Friday contain a seasonal upside edge. Now let's look at what has happened on the Monday after Thanksgiving.



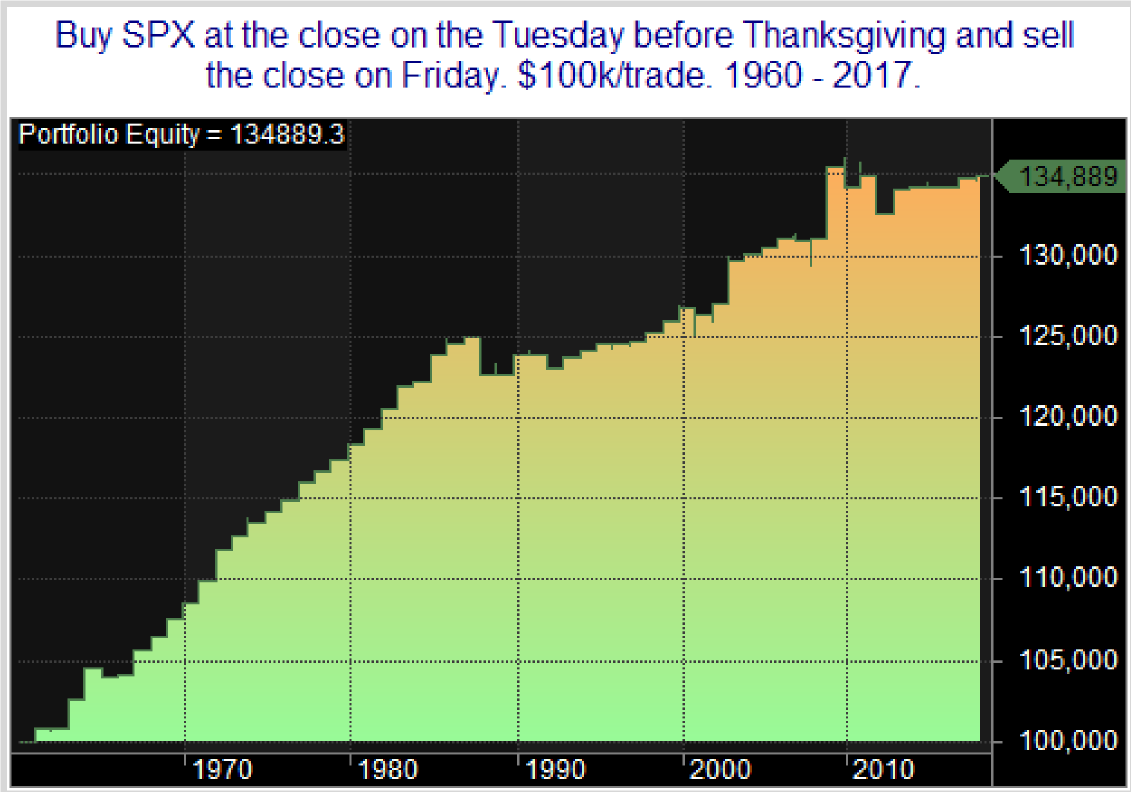

The numbers from the results table were extremely negative, but as you can see the downside edge has not been steady at all. While the trend has been down pretty much the entire time, a large portion of the downside move is thanks to a 9% drop in 2008. This suggests a seasonal downside edge does exist, but it is perhaps not as strong as the raw numbers would suggest.

With Wednesday and Friday both showing seasonal strength an obvious play would be to buy on Tuesday's close, and then sell at Friday's close. This strategy was first suggested by Yale Hirsch many years ago. I looked at it the last few years and have updated the results again below.

Buy SPX at the close on the Tuesday before Thanksgiving and sell the close on Friday. $100k/trade. 1960 - 2017.

| Statistics | |
|---|---|
| **All trades** | 58 |
| Avg. Profit/Loss | 601.54 |
| Avg. Profit/Loss % | 0.60% |
| Avg. Bars Held | 3.00 |
| Profit Factor | 5.23 |
| **Winners** | 49 (84.48 %) |
| Total Profit | 43145.69 |
| Avg. Profit | 880.52 |
| Avg. Profit % | 0.88% |
| Avg. Bars Held | 3.00 |
| Max. Consecutive | 22 |
| Largest win | 4531.19 |
| # bars in largest win | 3 |
| **Losers** | 9 (15.52 %) |
| Total Loss | -8256.43 |
| Avg. Loss | -917.38 |
| Avg. Loss % | -0.92% |
| Avg. Bars Held | 3.00 |
| Max. Consecutive | 2 |
| Largest loss | -2472.14 |
| # bars in largest loss | 3 |
| Max. trade drawdown | -2472.14 |
| Max. trade % drawdown | -2.47 |

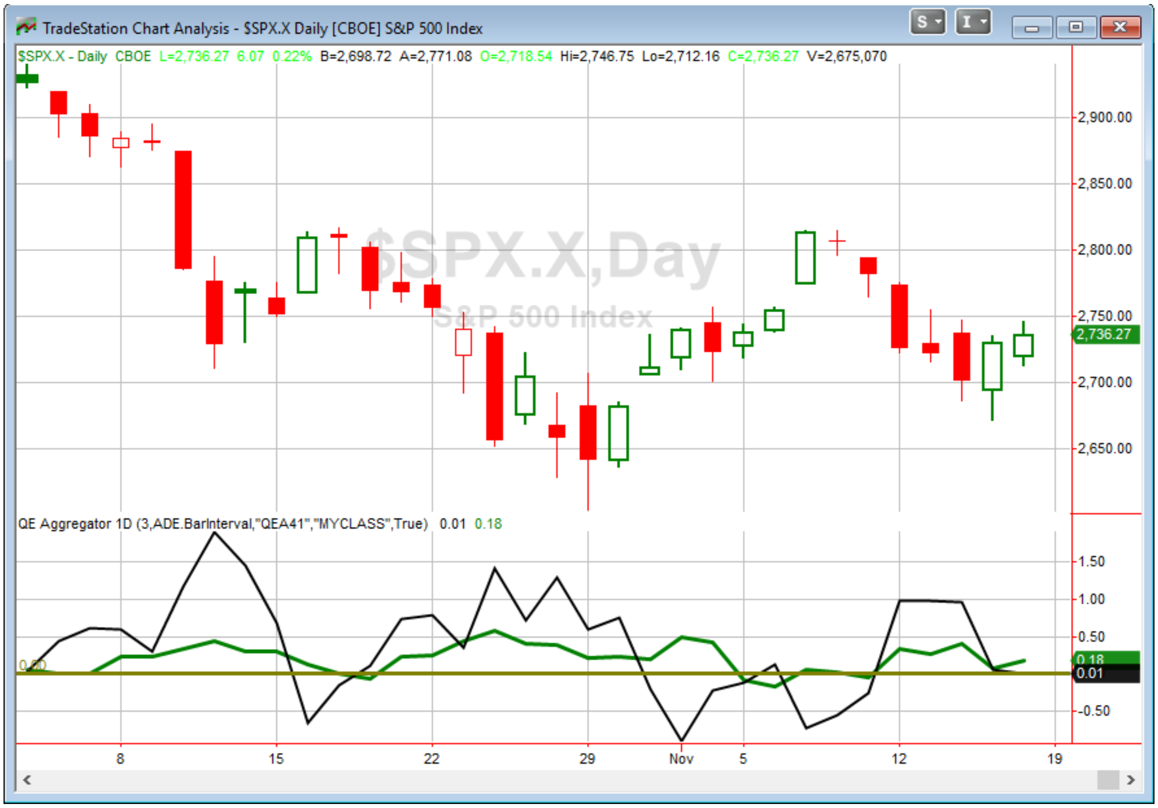
As you can see the numbers are extremely strong. Below is an equity curve.




From 1960 through 1986 this trade would've worked fantastically. There was only one year during this period when it would have failed to make money. From 1987 to the present it has continued to do well, but not to the same degree as it had before. There have in fact been seven losing years over this time period. Still, the curve looks nicely positive and traders could consider a trade along these lines if other indicators also seem to be lining up.

I will also note that there has been a vast difference in performance during recent times depending on how the market moved leading up to Wednesday. To examine this, I used SPY instead of SPX, because SPY has better intraday data. Since 1993, I found that years in which SPY closed in the top half of its intraday range on Thanksgiving Tuesday posted a 9-5 record from Tuesday's close to Friday's close. When SPY closed in the bottom half of its range on Tuesday the performance over Wednesday to Friday was 10-1. And the average instance posted a 0.8% gain these years versus a 0.1% average gain the other years. So Tuesday's action appears worth watching as we approach this potentially seasonally bullish period.

I have updated the Aggregator chart below.




Tonight the green Aggregator Line remained a little above zero. Positive readings mean net expectations are for upside over the next few days. Meanwhile, with SPX closing just under the Differential Pivot on Friday, the black Differential Line also held barely 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 zero. But with both lines so close to zero, this setup again barely qualifies. Still, the Aggregator signal stayed long at the close.

With the current active studies, expectations are slated to remain bullish on Monday. This could change if strong bearish evidence emerges. The Differential Pivot will be *inverted at* 2728.54 on Monday. That is 0.3% *below* Friday's close. An inverted pivot means that the Differential Line will cross through zero if SPX closes flat. In this case, SPX is going to need to close down at least 0.3% in order to remain oversold. Anything less than that and it will be considered "overbought" versus recent expectations as of Monday's close.

I generally view inverted pivots as opportune times to take profits. This is because upside is now limited. Short-term evidence remains a bit mixed. And while bullish seasonality will kick in in a few days, Monday and Tuesday don't show it. So I will look to exit my remaining SPY on Monday as long as I can get a good fill. I am not interested in selling into a large gap lower, because we still have a bullish Aggregator, and a move down of 0.3% or more would likely keep the Aggregator bullish. But if I can get out at Friday's close or better on Monday, then I will do so. Ideally, we would see a bit of a pullback on Monday and/or Tuesday to set us up for a potential Thanksgiving trade. But the market rarely cares about my "ideal" setups. So I'll wait to see what happens, and what additional evidence emerges and then I'll adjust my strategy accordingly.

***Intermediate-term Outlook (2 weeks – 2 months) – updated 11/19– slightly bullish***

| Combo #1 | Combo #2 | Combo #3 |
|---|---|---|
| Long | Long | Long |

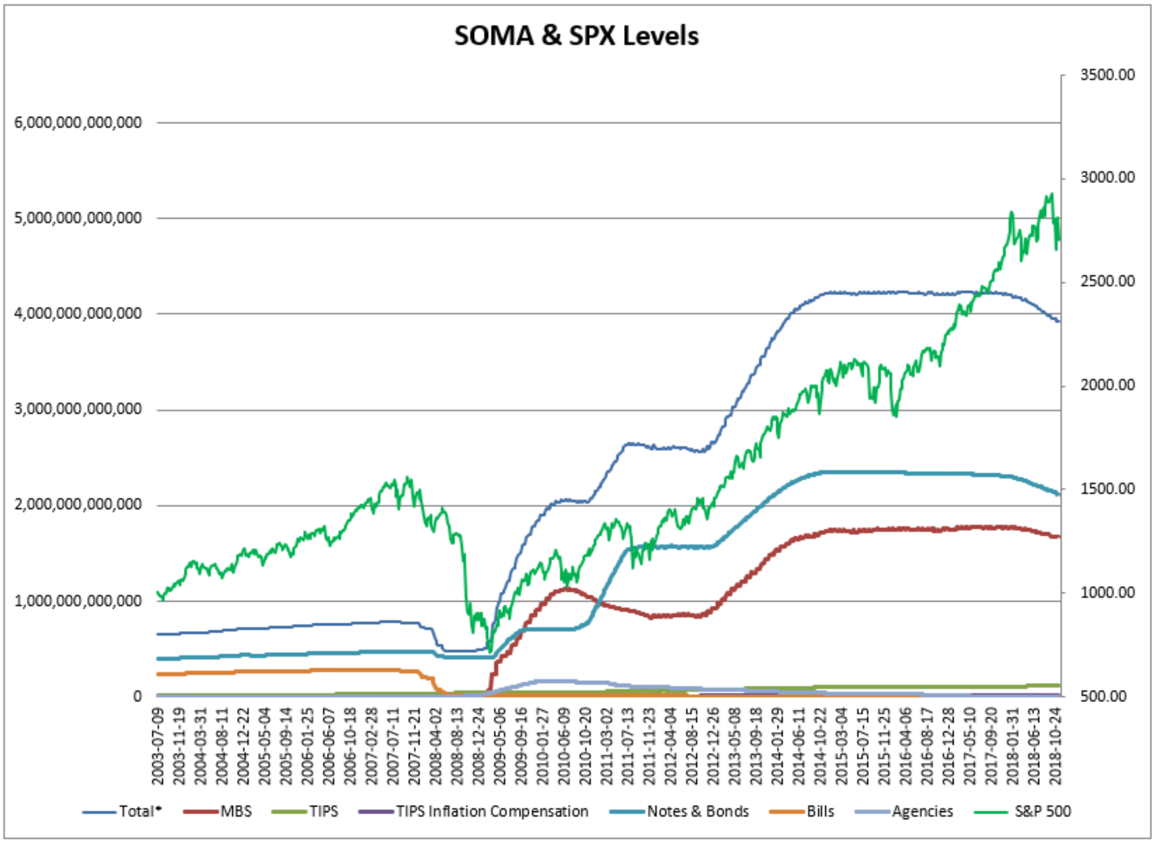
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the Quantifiable Edges Market Timing Course, which 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 the Combo Systems all remained "Long".*

This past week was a down one for the market. The SPX lost 1.6%, the NASDAQ declined 2.1% and the Russell 2000 had a 1.4% drop. There were no new studies that emerged this past week with intermediate-term significance.

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 is a long-term view of SOMA and SPX (back to 2003).*




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

« As of 11/07/2018

DOMESTIC SECURITIES HOLDINGS AS OF

**November 14, 2018**

Summary | T-Bills | T-Notes and T-Bonds | FRN | TIPS | Agencies

| Security Type | Total (in Thousands) |
|---|---|
| US Treasury Bills (T-Bills) | |
| US Treasury Notes and Bonds (Notes/Bonds) | 2,115,516,723.2 |
| US Treasury Floating Rate Notes (FRN) | 17,245,206.4 |
| US Treasury Inflation-Protected Securities (TIPS)* | 115,578,709.4 |
| Federal Agency Securities** | 2,409,000.0 |
| Agency Mortgage-Backed Securities*** | 1,670,824,668.7 |
| Total SOMA Holdings | 3,921,574,307.7 |
| Change From Prior Week | 1,782,974.6 |

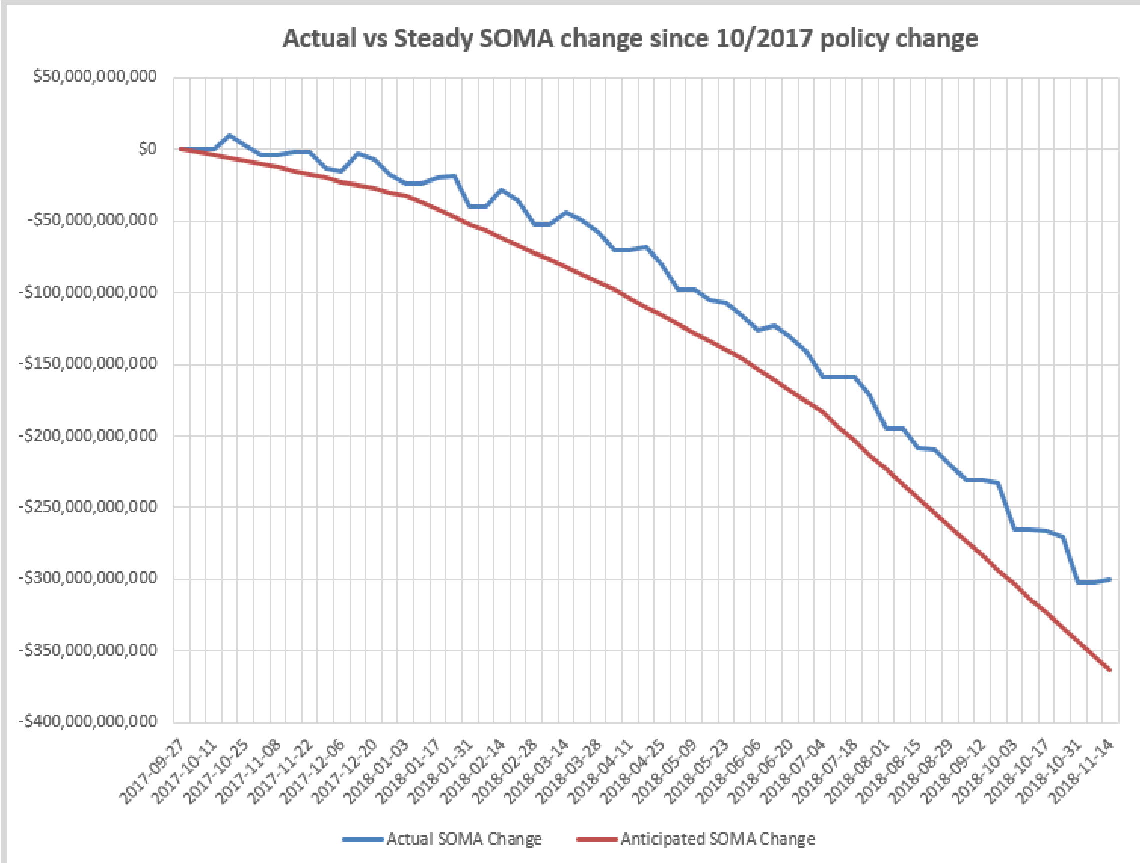
*Does not reflect inflation compensation of 22,079,735.1

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

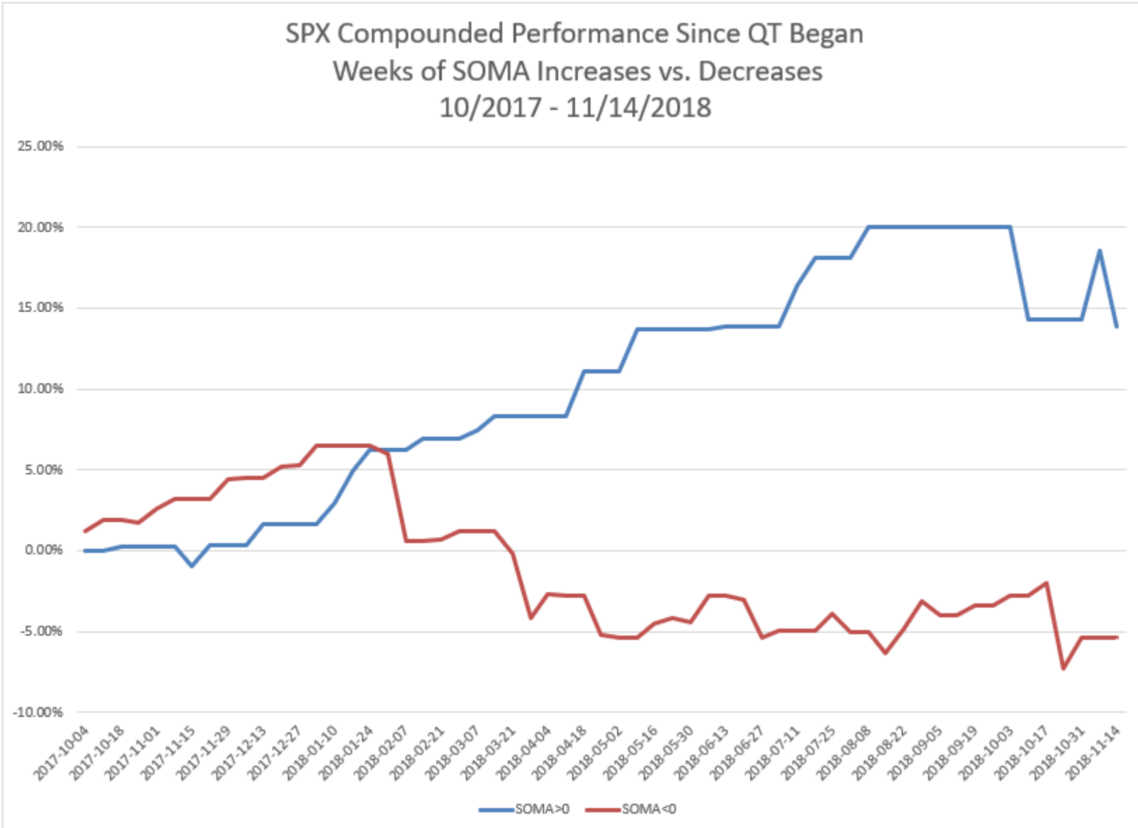
***Guaranteed by Fannie Mae, Freddie Mac, and Ginnie Mae. Current face value of the securities, which is the remaining principal balance of the securities.

*Data posted on 11/15/2018 4:30pm.*

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




The Fed's SOMA this past week (Wednesday to Wednesday) posted a gain of $1.7 billion. That is in line with expectations I laid out last week for a mild rise. But the modest liquidity inflow did not help out the bulls. The SPX fell a steep 4.0% during this week ending Wednesday 11/14. The "Actual vs Steady" chart shows that the rise in the SOMA this past week was opposite the norm with the Quantitative Tightening (QT) rate being $50 billion / month. Though it did not happen this past week, the market has typically encountered difficulty during SOMA contractions, 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 QT began of being long SPX during SOMA expansion weeks vs SOMA contraction weeks. It is updated from last week.




The lack of QT this past week meant movement in the blue "expansion week" profit curve. And after spiking up last week, it gave it back those gains this week. Despite the recent struggles, expansion weeks have seen strong gains over the last 13 months. Meanwhile weeks with QT (red line) have been net losers. Since October 2017 the blue "expansion week" strategy would have posted a 13.9% gain while the red "contraction week" strategy would have lost 5.35%. So how might the next few weeks of QT play out? Let's first look at the T-Note and T-Bond Maturity Table below, from the Fed's website.

« As of 11/07/2018

DOMESTIC SECURITIES HOLDINGS AS OF

**November 14, 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] |
|---|---|---|---|---|---|---|
| 11/15/18 | 912810EB0 | 9.000 | 3,842,000.0 | 53.55% | | |
| 11/15/18 | 912828M64 | 1.250 | 122,282.3 | 0.51% | | |
| 11/15/18 | 912828JR2 | 3.750 | 30,339,856.6 | 52.90% | | |
| 11/30/18 | 912828U40 | 1.000 | 2,767,228.7 | 9.62% | | |
| 11/30/18 | 912828A34 | 1.250 | 5,652,000.0 | 16.15% | | |
| 11/30/18 | 912828RT9 | 1.375 | 16,496,968.3 | 54.42% | | |
| 12/31/18 | 912828U99 | 1.250 | 3,457,357.0 | 11.74% | | |
| 12/31/18 | 912828RY8 | 1.375 | 12,695,123.4 | 42.41% | | |
| 12/31/18 | 912828A75 | 1.500 | 2,057,000.0 | 5.88% | | |

As you can see, there was a sizable treasury expiration on Thursday. So the market does have some QT to deal with this current week. (Of course bulls are hoping that some of the previous selling was in anticipation of that.) Therefore, we will see s substantial reduction in the SOMA this week.

But any QT for the week ending on the 28th will be due to AMBS securities rolling off the books. Compared to treasuries, AMBS flows are a little more difficult to anticipate. This is because 1) amounts may vary depending on loan pre-payments, and 2) there is a lag of 1-3 months to settle. For those interested in details, AMBS policies and procedures are described in more detail at the Fed's website: https://www.newyorkfed.org/markets/ambs-treasury-faq. I have found that examining past months will often provide clues as to the flows we can anticipate during similar periods of the current month. Based on past months, weeks ending on or around the 28th have generally seen a fairly strong amount of QT. I would expect no different this month.

And as we see above, there is another large treasury expiration at the end of November. So we are likely to see 3 weeks in a row of sizable QT.

Overall, intermediate-term studies are now leaning bullish. The seasonal strength is helping all three Market Timing Course combo systems remain bullish. The high CBI reading study from a few weeks ago suggested a bullish edge, and that will remain active through this week. And the FTD study from last week suggests that bounce is characteristic of one that will more often succeed than fail. But QT is still a concern. And QT is amping up here over the next few weeks. I could envision a scenario where the market dips some after Thanksgiving and in early December before we hit another strong seasonal period that aids the bulls through the end of 2018. I am keeping my intermediate-term outlook "slightly bullish". I am a bit more inclined to look for long opportunities than shorts, but am still willing to make short-term trades in either direction.

## Catapult and Capitulative Breadth Statistics

*Catapult & CBI Presentation Link*

***OpenCatapult Triggers***

GE – 1/3 @ $7.99 (bought @ limit)
SLB – 1/3 @ $47.34 (buy @ limit) – not filled, cancel for now
CELG – 1/3 @ $69.63 (bought @ limit)
***New***
WMT – 1/3 @ $97.69 (buy @ limit)

***Broad Market Large Cap CBI – 4(GE, SLB, CELG, WMT)***

## 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.*

***WMT – Buy 1/3 Catapult position @ $97.69 LIMIT***. From the Catapult and CBI section above, this is the 1st of up to 3 possible lots for WMT.

## Current Open Trade Ideas

| Symbol | Entry Date | Entry Price | Current Price | % Gain/Loss | Stop | Notes |
|---|---|---|---|---|---|---|
| QCOM(1/3) | 11/12/2018 | $56.37 | $55.88 | -0.87% | | *sell on open* |
| QCOM(1/3) | 11/13/2018 | $54.49 | $55.88 | 2.55% | | *sell on open* |
| GE(1/3) | 11/13/2018 | $7.99 | $8.02 | 0.38% | | Catapult |
| ***SPY(1/4)*** | ***11/13/2018*** | ***$272.57*** | ***$273.02*** | ***0.17%*** | | ***sold @ $273.02 LIMIT*** |
| SPY(1/4) | 11/14/2018 | $270.20 | $273.73 | 1.31% | | *sell @ $273.73 limit* |
| QCOM(1/3) | 11/14/2018 | $54.16 | $55.88 | 3.18% | | *sell on open* |
| CELG(1/3) | 11/15/2018 | $69.28 | $69.65 | 0.53% | | Catapult |

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