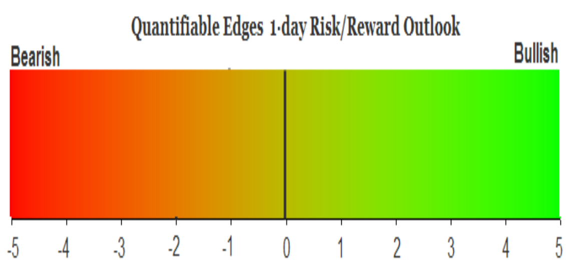
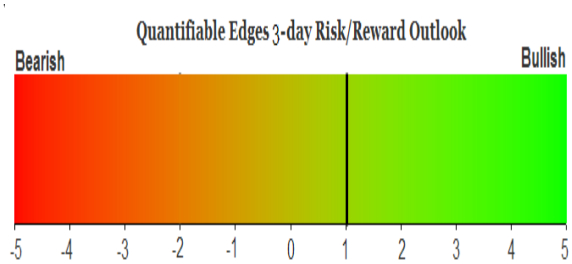
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

December 31, 2018 Volume 11 Issue 251

Market Overview





Signals Overview

Aggregator	CBI Reading
Flat	15

Tonight's Research Points

- The last day of the year used to be bullish, but the edge changed at the turn of the century.
- The last 15 minutes of the year normally sees a pullback – especially with smallcaps.
- Treasury expirations on Monday will cause a drop in the SOMA this week. But the week ending Wed the 9th could see a slight rise.

Short-term Outlook
The Bottom Line

It appears there could be more to the bounce, but the market remains short-term overbought thanks to Wednesday's huge move. Not a strong directional edge here, but more up than down.

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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						
December 28, 2018	Gap down then reverse up strong	1-2 days	Bearish			
December 27, 2018	100-low cls yest. 5th low low, then up 1%	1-4 days	Bullish			
December 27, 2018	Dn 1% to 50-low yest. Up 2day > 2 ago	1-5 days	Bullish			
December 24, 2018	SPX down 1.5% for 3 days	1-8 days	Bullish			
Active - Long Term						
December 21, 2018	CBI 10+. SPX 50-day low.	1-18 days	Bullish			
November 1, 2018	Best 6 Month During Pres Yr 3	1-6 months	Bullish	17.70%	-3.10%	-7.20%
October 1, 2018	Quantitative Tightening $50billion/mo	int term	Bearish			

The Evidence

Friday saw a lot of back and forth, and then it finished mixed. The SPX declined 0.1%, the NASDAQ rose 0.1%, and the Russell 2000 gained 0.5%. Breadth was positive as the NYSE Up Issues % was 60% and the Up Volume % came in at 51%. NYSE volume declined some from Thursday’s level.

There were a couple of price-action based studies that triggered in the Quantifinder, but when I looked at them within the context of the current market environment (downtrending, volatile, etc) they did not appear to offer much of an edge. So I have not included them in this report. There were some interesting seasonal studies, though.

While the last day of the year used to be a bullish day for the market, that seems to have changed since the turn of the century. This is true across a number of indices. The most dramatic example is the NASDAQ, which I highlighted last year in the 12/29/17 letter. I have updated the chart below.

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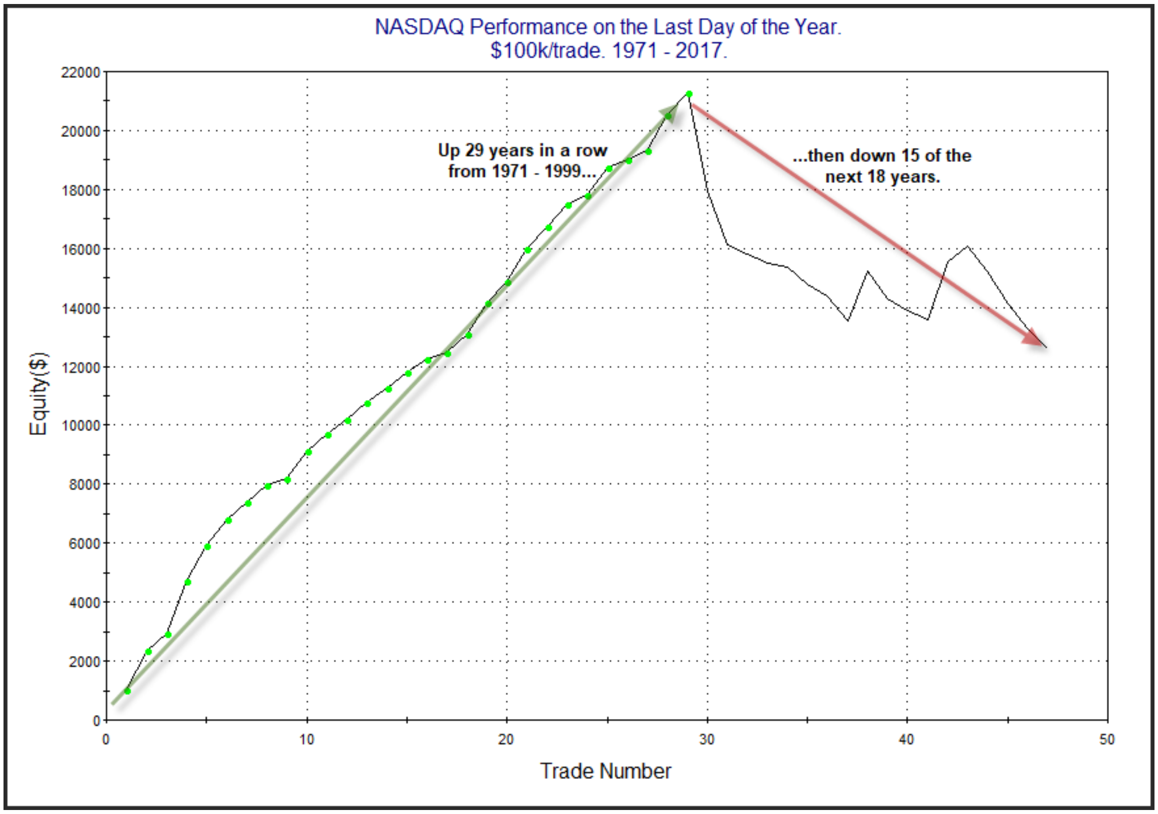


Closing up 29 years in a row is fairly astounding. Just as astounding is the abrupt reversal and move lower for 15 of the next 18 years. I have no good explanation for why such a formerly consistent edge changed, but it did.

The Nasdaq study is a great reminder though. The market is constantly changing and evolving. 2019 is just a few trading hours away. I'm not sure what it has in store for us, but I know it will play out in its own unique pattern. We will see clues along the way, and many of the truisms we've identified through studies over the last 11 years at Quantifiable Edges will continue to work. But some may flounder. And when something stops working, like the "last day of year bullishness" above, then I will do my best to recognize it early. Examining edges is more than just running numbers. The profit curves are so vital. Over the last several years I have seen this point driven home time and again through my research. This is why I so often take the time to show the profits curves in the subscriber letter.

In another study I last showed in the 12/29/17 letter I found the returns in the last 15 minutes of the year to be especially interesting. I have updated that study below.

SPY Performance in the last 15 minutes of the YEAR.
$100k/trade. 1998 - 2017.

TradeStation Performance Summary Expand

All Trades

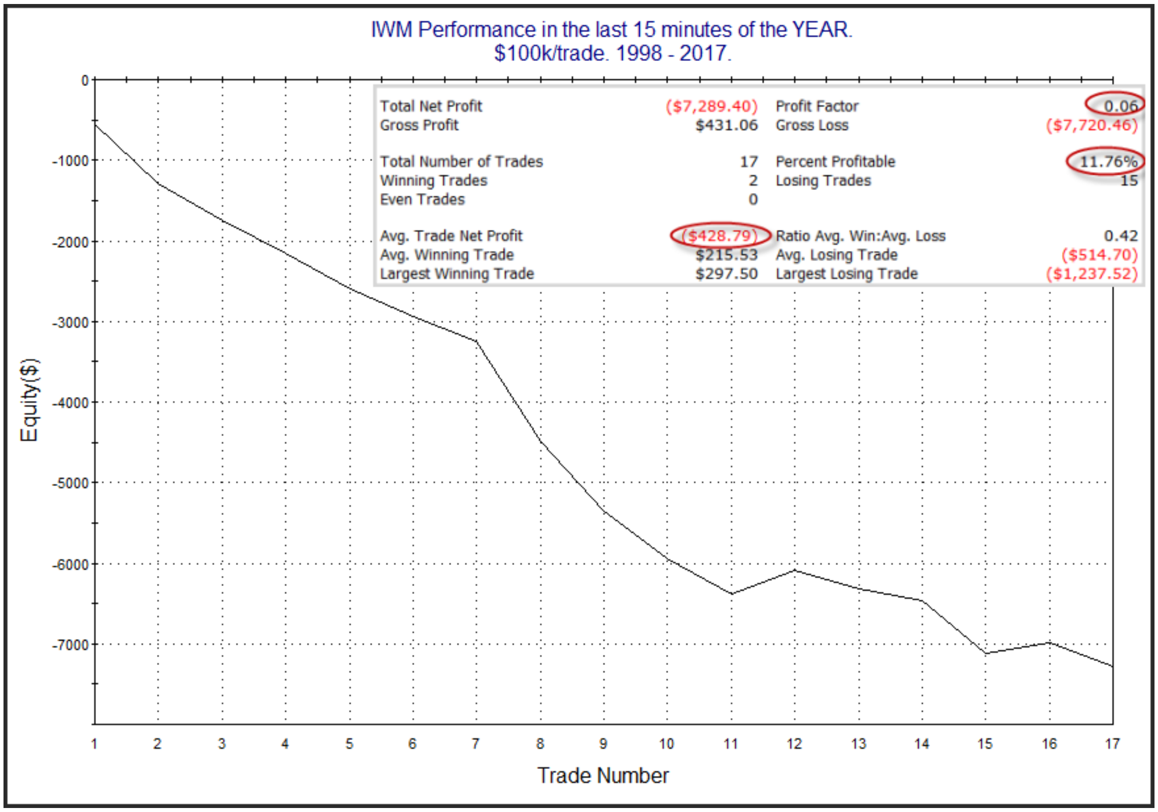
Total Net Profit	($4,282.37)	Profit Factor	0.16
Gross Profit	$840.52	Gross Loss	($5,122.89)
Total Number of Trades	20	Percent Profitable	20.00%
Winning Trades	4	Losing Trades	16
Even Trades	0		
Avg. Trade Net Profit	($214.12)	Ratio Avg. Win:Avg. Loss	0.66
Avg. Winning Trade	$210.13	Avg. Losing Trade	($320.18)
Largest Winning Trade	$415.36	Largest Losing Trade	($654.48)

The numbers here are very strong. The average trade has seen SPY drop over 0.2%, and the average losing trade has seen it close down 0.32%. That's a sizable average move for a 15-minute period. Below is a list of all the instances.

SPY Performance in the last 15 minutes of the YEAR. $100k/trade. 1998 - 2017.				
Date/Time	**Signal**	**Price**	**% Profit**	**Run-up Drawdown**
12/31/1998 15:45	Buy	$123.69	-0.65%	$153.52
12/31/1998 16:00	Sell#2	$122.88		($808.00)
12/31/1999 12:45	Buy#2	$147.31	-0.21%	$67.80
12/31/1999 13:00	Sell	$147.00		($318.66)
12/29/2000 15:45	Buy	$132.47	-0.17%	$22.62
12/29/2000 16:00	Sell#2	$132.25		($444.86)
12/31/2001 15:45	Buy	$115.58	-0.60%	$8.65
12/31/2001 16:00	Sell#2	$114.89		($631.45)
12/31/2002 15:45	Buy	$88.11	0.06%	$90.72
12/31/2002 16:00	Sell#2	$88.16		($181.44)
12/31/2003 15:45	Buy	$111.45	-0.27%	$26.91
12/31/2003 16:00	Sell#2	$111.15		($269.10)
12/31/2004 15:45	Buy	$121.28	-0.20%	$8.24
12/31/2004 16:00	Sell#2	$121.04		($206.00)
12/30/2005 15:45	Buy	$125.03	-0.34%	$23.97
12/30/2005 16:00	Sell#2	$124.60		($375.53)
12/29/2006 15:45	Buy	$141.91	-0.29%	$49.28
12/29/2006 16:00	Sell#2	$141.50		($295.68)
12/31/2007 15:45	Buy	$147.04	-0.42%	$6.80
12/31/2007 16:00	Sell#2	$146.42		($462.40)
12/31/2008 15:45	Buy	$90.59	-0.40%	$77.21
12/31/2008 16:00	Sell#2	$90.23		($606.65)
12/31/2009 15:45	Buy	$111.96	-0.46%	$8.93
12/31/2009 16:00	Sell#2	$111.44		($473.29)
12/31/2010 15:45	Buy	$125.81	-0.02%	$7.94
12/31/2010 16:00	Sell#2	$125.79		($230.26)
12/30/2011 15:45	Buy	$126.00	-0.33%	$0.00
12/30/2011 16:00	Sell#2	$125.59		($325.13)
12/31/2012 15:45	Buy	$141.87	0.42%	$485.76
12/31/2012 16:00	Sell#2	$142.46		($7.04)
12/31/2013 15:45	Buy	$184.31	0.14%	$200.54
12/31/2013 16:00	Sell#2	$184.56		($16.26)
12/31/2014 15:45	Buy	$206.14	-0.30%	$4.85
12/31/2014 16:00	Sell#2	$205.52		($363.75)
12/31/2015 15:45	Buy	$204.58	-0.32%	$68.32
12/31/2015 16:00	Sell#2	$203.92		($346.48)
12/30/2016 15:45	Buy	$223.02	0.23%	$241.92
12/30/2016 16:00	Sell#2	$223.54		($76.16)
12/29/2017 15:45	Buy	$267.28	-0.15%	$48.62
12/29/2017 16:00	Sell#2	$266.88		($239.36)

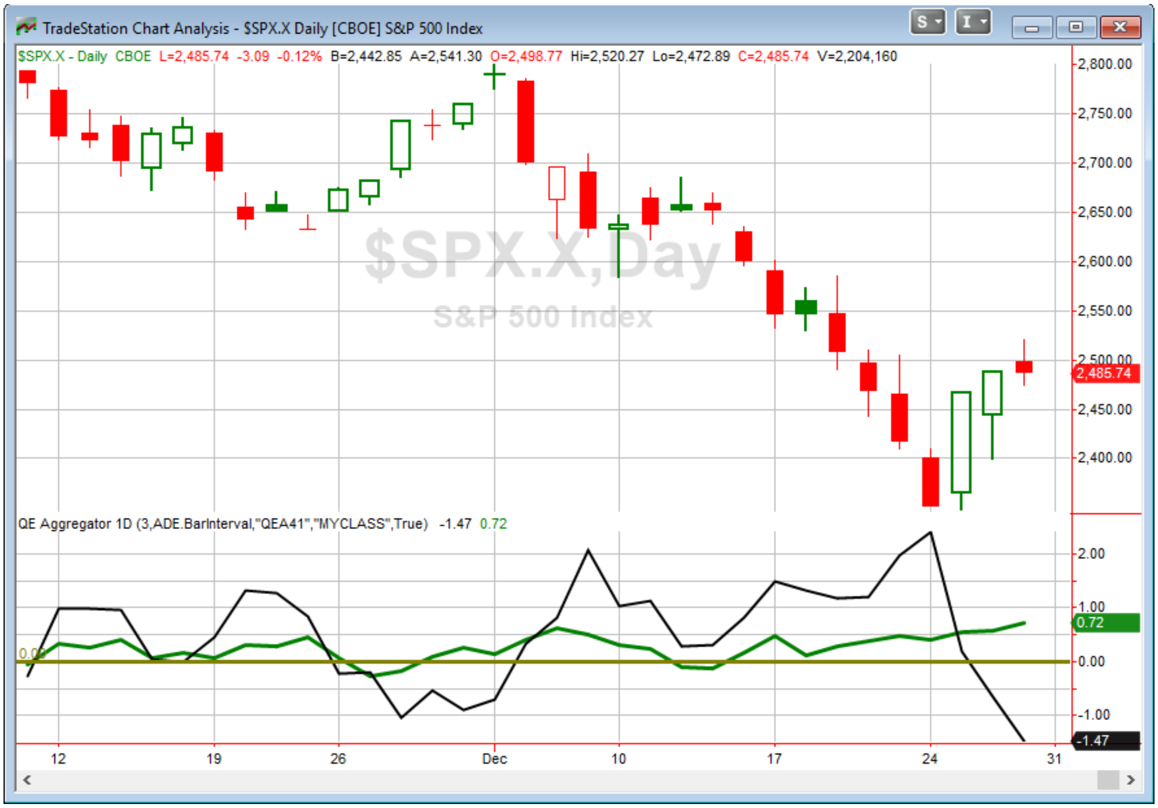
Three of the last six years have bucked the trend and closed up. Prior to that the results were *extremely* bearish.

IWM has shown an even stronger tendency to sell off heading into the last 15 minutes of the year. But its history is not as long, so I could only run it back to 2001. Below are those results.



I suspect there are a lot of portfolio adjustments that are made by institutions as we approach the close on the last day of the year, and this may be the reason that the indices, especially smallcaps, have seen a decline. Whether it is an up or down year does not seem to have an impact on the results. Looking at years like 2000, 2001, and 2008, they were all down in the last 15 minutes. Just a little quirk you may want to keep in mind as we approach the close on Monday.

I have updated the Aggregator chart below.



Today the green Aggregator Line remained above zero. Positive readings mean net expectations are for upside over the next few days. Meanwhile, the black Differential Line remained 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 zero. Therefore, the Aggregator signal stayed flat at the close.

With the current active studies, expectations are slated to remain bullish on Monday. It would take very compelling new bearish evidence to change this. The Differential Pivot will be *inverted at* 2503.36 on Monday. That is 0.7% *above* Friday's close. An inverted pivot means that the Differential Line will cross through 0 if SPX closes flat. In this case, SPX is going to need to close up at least 0.7% in order to remain overbought vs recent expectations. Anything less than that and it will be considered oversold as of Monday's close.

Friday's action did not do anything to change my overall outlook. The Aggregator is neutral, though it could easily turn bullish on Monday. The Quantifiable Edges Capitulative Breadth Indicator (CBI) dropped from 26 to 15 on Friday. Fifteen is still a large number that suggests there are still plenty of stocks left with further bounce in them. When coming off a deeply oversold condition with a CBI spike, I generally like to try and keep a small amount of index exposure until the CBI returns to a more neutral state (around 3-5). I took off most of my index exposure on Thursday and Friday, but still have one lot of SPY, and I will continue to hold that a little longer. I will also be especially careful about shorting until we get a normalization of the CBI. Overbought after a large scale selloff into an intermediate-term low has a greater ability to become more overbought than most other situations. That is where the market is now. I may be looking to add shorts in the coming days and weeks, but not yet.

Intermediate-term Outlook (2 weeks – 2 months) – updated 12/31– neutral

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

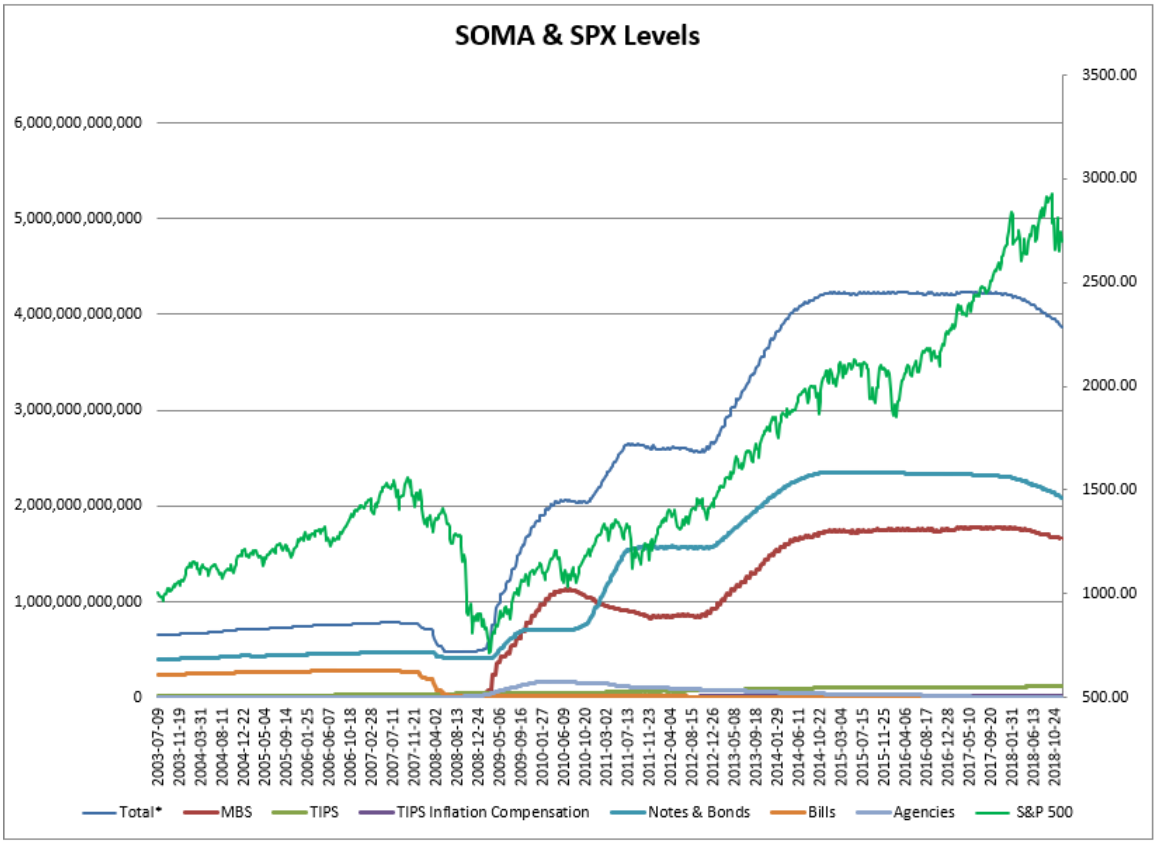
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the Quantifiable Edges Market Timing Course, which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

Thanks to Wednesday's massive up day, the market put in strong gains for the week. The SPX rose 2.9%, the NASDAQ rallied 4.0%, and the Russell 2000 jumped 3.5%. The strong moves this week were reactive to the strongly oversold condition coming into the week. They did not trigger anything yet with intermediate-term implications. We typically will see possible evidence of rally success / failure odds a little after the initial bounce occurs.

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 12/19/2018

DOMESTIC SECURITIES HOLDINGS AS OF
December 26, 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)	2,082,970,091.9
US Treasury Floating Rate Notes (FRN)	18,825,874.1
US Treasury Inflation-Protected Securities (TIPS)*	116,544,672.9
Federal Agency Securities**	2,409,000.0
Agency Mortgage-Backed Securities***	1,637,123,400.3
Total SOMA Holdings	3,857,873,039.2
Change From Prior Week	-11,563,317.7

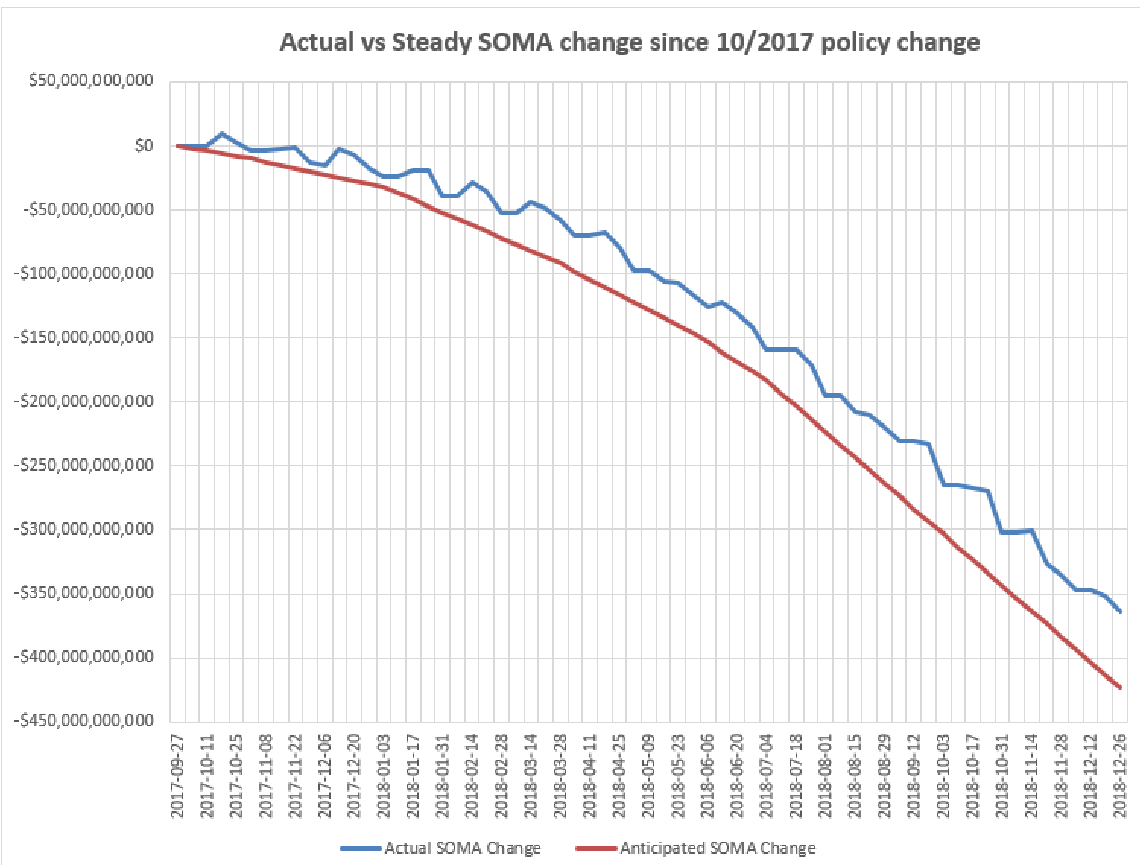
*Does not reflect inflation compensation of 22,376,016.3

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

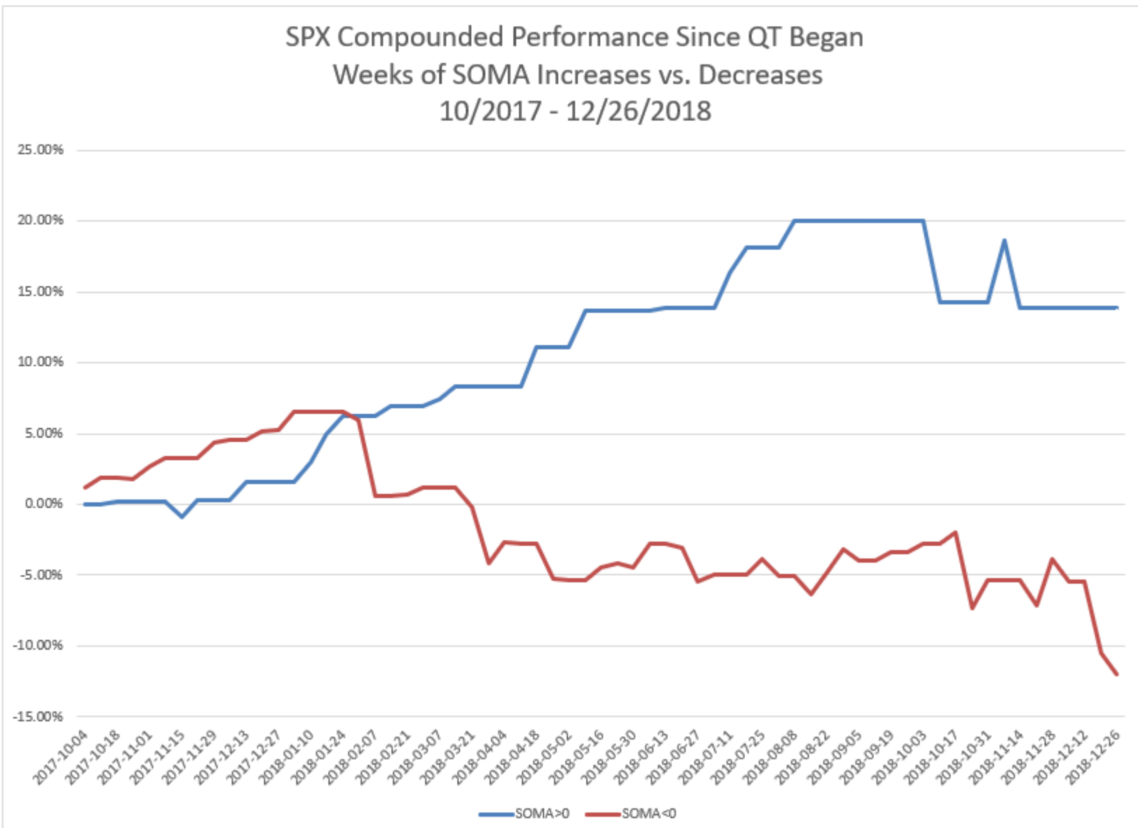
***Guaranteed by Fannie Mae, Freddie Mac, and Ginnie Mae. Current face value of the securities, which is the remaining principal balance of the securities.

Data posted on 12/27/2018 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) saw a decline of about $11.6 billion. That was expected as I laid out the last couple of weeks. Meanwhile, the SPX lost 1.6% for the week ending 12/26. That is a good sized drop. The "Actual vs Steady" chart shows that the $11.6 billion SOMA decline is about average with the Quantitative Tightening (QT) rate being $50 billion / month. 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.



You can see here the sharp contrast in expansion weeks versus contraction weeks over the last 15 months. Despite some recent struggles, expansion weeks (blue line) have seen strong gains. 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 11.9%. That is a substantial difference in performance. 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 11/28/2018

DOMESTIC SECURITIES HOLDINGS AS OF
December 5, 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]
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%		
1/31/19	912828V56	1.125	1,648,772.7	5.96%		
1/31/19	912828SD3	1.250	5,843,714.5	19.78%		
1/31/19	912828B33	1.500	4,173,000.0	11.92%		
2/15/19	912810EC8	8.875	7,497,000.0	57.27%		
2/15/19	912828P53	0.750	1,884,490.1	7.28%		
2/15/19	912828KD1	2.750	34,141,943.8	58.19%		
2/28/19	912828W30	1.125	3,605,863.3	12.18%		
2/28/19	912828SH4	1.375	6,315,645.0	21.48%		
2/28/19	912828C24	1.500	2,607,325.5	7.43%		

The first thing to note about the table above is that we have some treasuries maturing on Monday, 12/31. So this week will certainly see a substantial decline for the SOMA. But the next set of expirations is not until 1/31/19. So any QT between now and then will be due to AMBS securities coming 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.

The last 4 weeks ending on the 8th, 9th, or 10th occurred in October, August, May, and January, and they all saw slight increases in the SOMA. November 8th 2017 did see a slight decline. Still, it appears unlikely that the week ending on 1/9/19 will see much QT. And I expect there may even be a slight SOMA increase.

I don't have a lot of clarity for the intermediate-term at this point. On the plus side, we are in a strong seasonal period (best 6 months during 3rd presidential year), and the CBI spike and severe oversold condition are normally enough that a multi-week bounce follows. But Fed policies remain a concern and we will need to see some upside followthrough and sustained buying to turn this downtrend into an uptrend. Two good days (Wed and Thurs) are not enough to declare a bottom and a new emerging bull just yet. I am keeping my bias neutral. I am willing to take trades in either direction. And I expect to see opportunities in both directions in the coming weeks, especially if the market continues to overreact to every bit of news. For me, this is now a time to generally keep time-frames short and be nimble with my mindset and my trading.

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

OpenCatapult Triggers

SLB – 1/3 @ $37.84 (bought @ limit)
SLB – 1/3 @ $37.79 (bought @ limit)
AGN – 1/3 @ $136.56 (bought @ limit)
SLB – 1/3 @ $36.20 (bought @ limit)
RTN – 1/3 @ $157.95 (bought @ limit)
AGN – 1/3 @ $135.63 (bought @ limit)
RTN – 1/3 @ $151.52 (bought @ limit)
AGN – 1/3 @ $131.46 (bought @ limit)
HAL – 1/3 @ $25.85 (bought @ limit)
OXY – 1/3 @ $59.98 (bought @ limit)
AAPL – 1/3 @ $146.83 (buy @ limit)
HAL – 1/3 @ $25.14 (buy @ limit)
OXY – 1/3 @ $57.11 (buy @ limit)
RTN – 1/3 @ $146.67 (buy @ limit)
USB – 1/3 @ $43.76 (buy @ limit)

Broad Market Large Cap CBI – 15(SLB-3, AGN-3, RTN-3, HAL-2, OXY-2, AAPL, USB)

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

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Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Pri	% Gain/Los	Stop	Notes
SPY(1/4)	12/17/2018	$259.40	$247.75	-4.49%		Aggregator
EMR(1/3)	***12/18/2018***	***$58.72***	***$59.50***	***1.33%***		***sold on open***
IWM(1/4)	***12/18/2018***	***$136.85***	***$132.48***	***-3.19%***		***sold on open***
EMR(1/3)	***12/19/2018***	***$58.49***	***$59.50***	***1.73%***		***sold on open***
FOXA(1/3)	12/19/2018	$48.78	$47.97	-1.66%		***sell on open***
SLB(1/3)	12/19/2018	$37.84	$36.60	-3.28%		Catapult
SLB(1/3)	12/20/2018	$37.34	$36.60	-1.98%		Catapult
EMR(1/3)	***12/20/2018***	***$57.22***	***$59.50***	***3.98%***		***sold on open***
AGN(1/3)	12/20/2018	$135.00	$132.80	-1.63%		Catapult
IWM(1/4)	***12/21/2018***	***$131.79***	***$132.43***	***0.49%***		***sold on close***
SLB(1/3)	12/21/2018	$35.47	$36.60	3.19%		Catapult
AGN(1/3)	12/21/2018	$135.20	$132.80	-1.78%		Catapult
C(1/3)	12/21/2018	$51.90	$51.83	-0.13%		***sell on open***
FOXA(1/3)	12/21/2018	$48.00	$47.97	-0.06%		***sell on open***
KHC(1/3_	12/21/2018	$44.85	$43.57	-2.85%		***sell on open***
RTN(1/3)	12/21/2018	$151.01	$152.92	1.26%		Catapult
C(1/3)	12/24/2018	$49.40	$51.83	4.92%		***sell on open***
FOXA(1/3)	12/24/2018	$46.90	$47.97	2.28%		***sell on open***
KHC(1/3_	12/24/2018	$44.05	$43.57	-1.09%		***sell on open***
RTN(1/3)	12/24/2018	$150.15	$152.92	1.84%		Catapult
AGN(1/3)	12/24/2018	$129.99	$132.80	2.16%		Catapult
HAL(1/3)	12/24/2018	$25.61	$26.46	3.32%		Catapult
OXY(1/3)	12/24/2018	$59.42	$60.47	1.77%		Catapult
AAPL(1/3)	12/26/2018	$146.83	$156.23	6.40%		Catapult
C(1/3)	12/26/2018	$49.26	$51.83	5.22%		***sell on open***
FDX(1/3)	12/26/2018	$152.70	$158.98	4.11%		***sell on open***
HAL(1/3)	12/26/2018	$25.14	$26.46	5.25%		Catapult
HON(1/3)	12/26/2018	$124.83	$130.76	4.75%		***sell on open***
KHC(1/3)	12/26/2018	$42.54	$43.57	2.42%		***sell on open***
OXY(1/3)	12/26/2018	$57.11	$60.47	5.88%		Catapult
RTN(1/3)	12/26/2018	$146.67	$152.92	4.26%		Catapult
USB(1/3)	12/26/2018	$43.76	$45.21	3.31%		Catapult

Several Catapults reached their exit triggers and will be sold at the open on Monday. Several more could reach their exit targets on Monday.