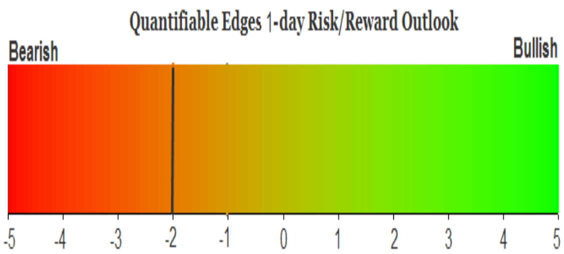
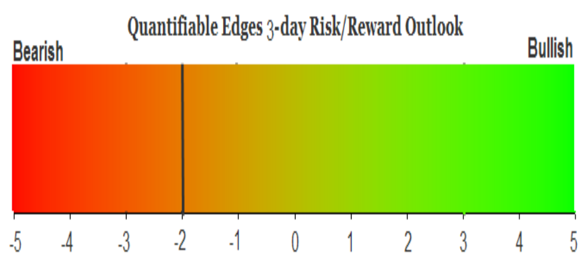
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 22, 2018 Volume 12 Issue 14

Market Overview





Signals Overview

Aggregator	CBI Reading
Short	0

Tonight's Research Points

- 3 days of strong NASDAQ breadth are often followed by a down day.
- MLK week has been negative over the long run, but not consistent, especially of late.
- SPY's gap and follow-through action on Friday suggests a pullback on Tuesday.
- NASDAQ's recent streak of higher closes suggests a pullback is likely.
- QT should be light this week (through Wednesday). Then we should see more sizable numbers in the 2 weeks that follow.

Short-term Outlook

The Bottom Line

The Aggregator is bearish and so am I...again.

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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						
January 22, 2019	Unfl gap up 0.5%-1%. Close > open < 20(	1 day	Bearish			
January 22, 2019	NASDAQ up 4 below 200ma	1-2 days	Bearish			
January 22, 2019	NASDAQ breadth 3:2 up 3x	1 day	Bearish			
January 18, 2019	SPY 3 days up 20-high < 200ma	1-2 days	Bearish			
Active - Long Term						
January 9, 2019	Up Issues > 70% for 3 days	1-85 days	Bullish			
January 9, 2019	SPY up 3 < 200. SPY volume dn 3.	1-20 days	Bearish			
January 8, 2019	Zweig Thrust	1-20 days	Bullish	7.50%	-1.45%	-2.50%
January 2, 2019	NASDAQ leading	int term	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			
Dropped Tonight						
December 21, 2018	CBI 10+. SPX 50-day low.	1-18 days	Bullish			
January 17, 2019	SPX up < 0.25% &<200. VIX up midwk.	1-2 days	Bearish			
January 14, 2019	Jan opex week weak	1-5 days	Bearish			

The Evidence

Friday was another rally day. The SPX finished the day up 1.3% the NASDAQ rose 1.0%, and the Russell 2000 gained 1.0%. Breadth was positive as the NYSE Up Issues % was 74% and the Up Volume % came in at 84%. NYSE volume rose. There was a positive influence on volume from it being opex Friday, but a negative influence from the upcoming long weekend.

Martin Luther King Jr. week has been an interesting one over the years for the stock market. The 1st year that the NYSE closed on MLK Day was 1998. The study below looks at the performance from the close of the Friday prior to MLK Day to the close of the Friday afterwards.

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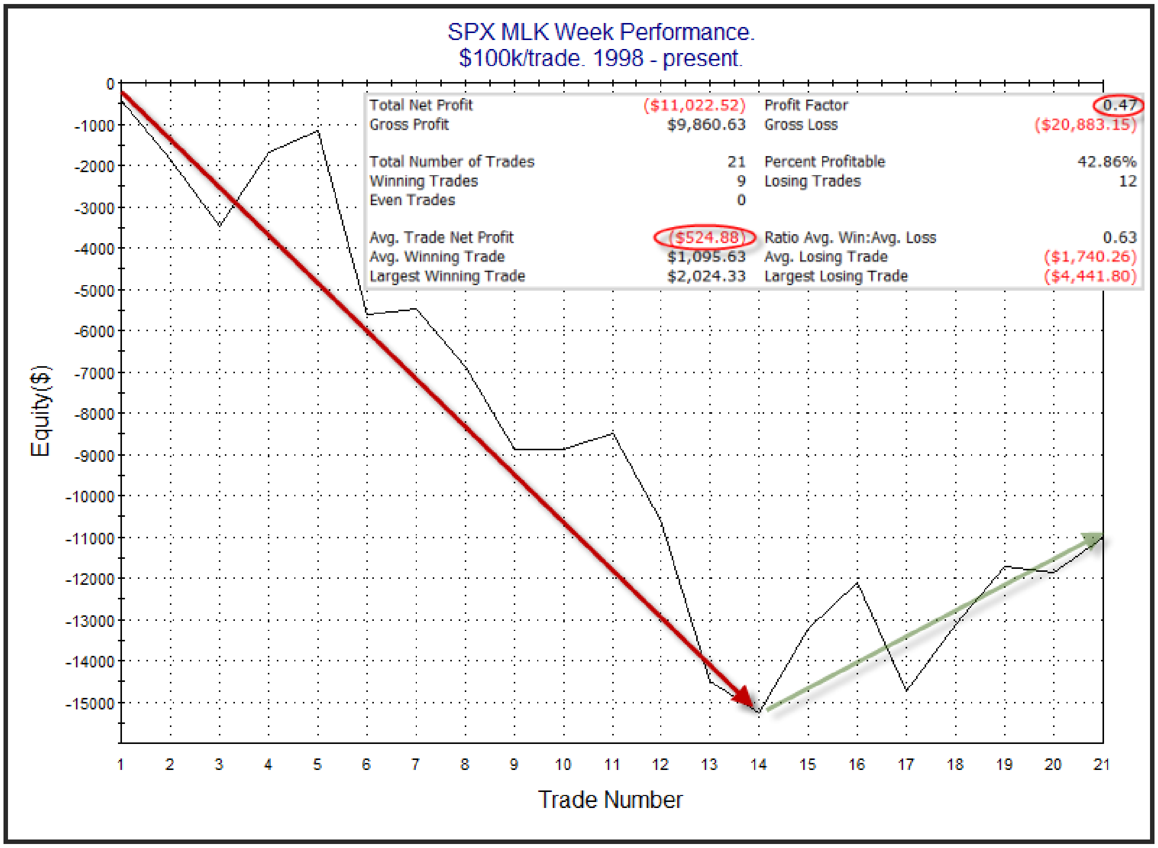

Over the 1st 14 years there appeared to be a bearish inclination during this week. That inclination has not played out over the last 7 years, though. I do not find the numbers and charts to be compelling enough to factor into my decision making. Shorter-term looks (1, 2, or 3 days) also do not appear to suggest a reliable edge.

One study that provided some compelling results is the one below. It was last seen in the 3/22/16 subscriber letter. It looks at other instances in which the NASDAQ rose exactly 4 days in a row and closed under the 200ma. All results have been updated.

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NASDAQ closes higher for exactly the 4th day in a row. It did NOT close at a 50-day low 4 days ago. Close < 200ma. Buy on close. Sell X days later. $100k/trade. 2002 - 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
10	-42,507.45	21	7	14	33.33	2,032.14	4,498.82	-4,052.32	-9,279.70	0.50	0.25	-2,024.16
9	-36,374.91	21	8	13	38.10	1,611.16	3,123.20	-3,789.55	-7,688.92	0.43	0.26	-1,732.14
8	-28,786.87	22	10	12	45.45	1,626.26	3,823.79	-3,754.13	-7,746.48	0.43	0.36	-1,308.49
7	-30,313.42	23	9	14	39.13	1,490.70	3,529.97	-3,123.55	-5,934.18	0.48	0.31	-1,317.97
6	-34,768.09	23	8	15	34.78	1,184.02	4,086.93	-2,949.35	-6,362.65	0.40	0.21	-1,511.66
5	-23,156.66	24	9	15	37.50	1,189.30	2,029.98	-2,257.36	-5,753.20	0.53	0.32	-964.86
4	-17,052.32	24	10	14	41.67	950.77	1,870.87	-1,897.14	-4,907.27	0.50	0.36	-710.51
3	-17,773.79	24	9	15	37.50	1,252.04	2,032.68	-1,936.15	-4,090.24	0.65	0.39	-740.57
2	-20,594.50	24	10	14	41.67	738.38	2,042.04	-1,998.45	-5,242.88	0.37	0.26	-858.10
1	-14,130.07	24	9	15	37.50	603.61	1,809.18	-1,304.17	-3,232.00	0.46	0.28	-588.75

All 24 instances closed below the entry price
at some point in the next week.

Results here appears to be strongly bearish. And the edge persists for up to 2 weeks. I also examined how the SPX might have performed when the Nasdaq had set up this way. The updated results below show this.

NASDAQ closes higher for exactly the 4th day in a row. It did NOT close at a 50-day low 4 days ago. Close < 200ma. Buy ***SPX*** on close. Sell X days later. $100k/trade. 2002 - 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
10	-28,471.99	21	5	16	23.81	3,851.87	7,245.00	-2,983.21	-7,631.40	1.29	0.40	-1,355.81
9	-24,968.87	21	9	12	42.86	1,941.80	4,733.40	-3,537.09	-5,350.02	0.55	0.41	-1,188.99
8	-20,490.93	22	8	14	36.36	1,988.57	6,129.50	-2,599.97	-7,676.64	0.76	0.44	-931.41
7	-20,357.05	23	9	14	39.13	1,674.55	4,320.55	-2,530.57	-6,238.08	0.66	0.43	-885.09
6	-24,735.18	23	6	17	26.09	1,988.74	4,716.15	-2,156.92	-5,959.76	0.92	0.33	-1,075.44
5	-18,017.53	24	10	14	41.67	998.83	1,915.14	-2,000.42	-6,523.10	0.50	0.36	-750.73
4	-13,552.10	24	10	14	41.67	751.34	1,659.08	-1,504.68	-4,056.12	0.50	0.36	-564.67
3	-14,847.98	24	12	12	50.00	704.33	1,802.76	-1,941.66	-5,547.24	0.36	0.36	-618.67
2	-19,319.52	24	9	15	37.50	490.42	1,695.10	-1,582.22	-5,495.94	0.31	0.19	-804.98
1	-10,040.56	24	9	15	37.50	574.84	1,736.36	-1,014.28	-3,300.30	0.57	0.34	-418.36

All 24 instances closed below the entry price
at some point in the next week.

Though not quite as powerful, these results appear just as consistently bearish as the NASDAQ results. Below is an equity curve that assumes a 2-day holding period.

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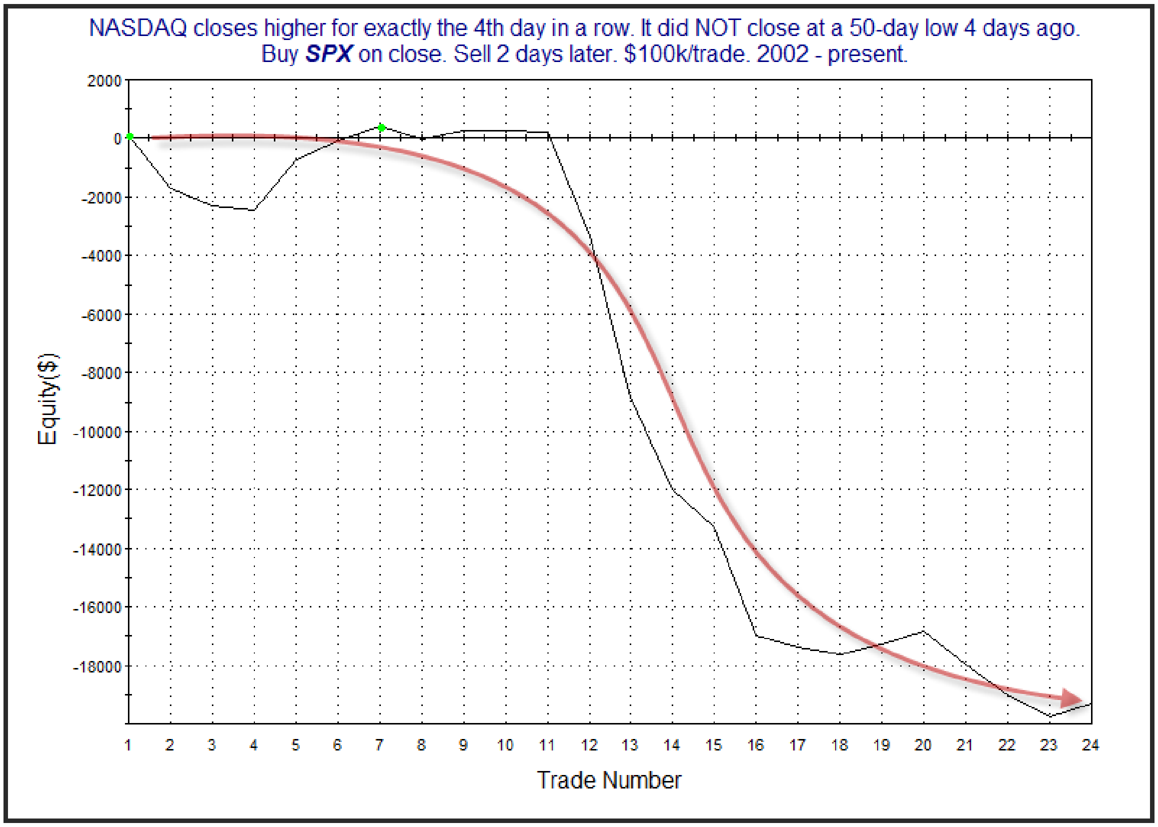

Certainly not the straightest curve we have seen, but it does wind its way from upper left to lower right. And the fact that both the NASDAQ and the SPX have closed below the entry price in every instance has me accepting of this study and including it on the Active List.

The one below looks at NASDAQ breadth, and also suggests bearish implications. It last appeared Thursday night in the 1/18/19 letter and has been updated.

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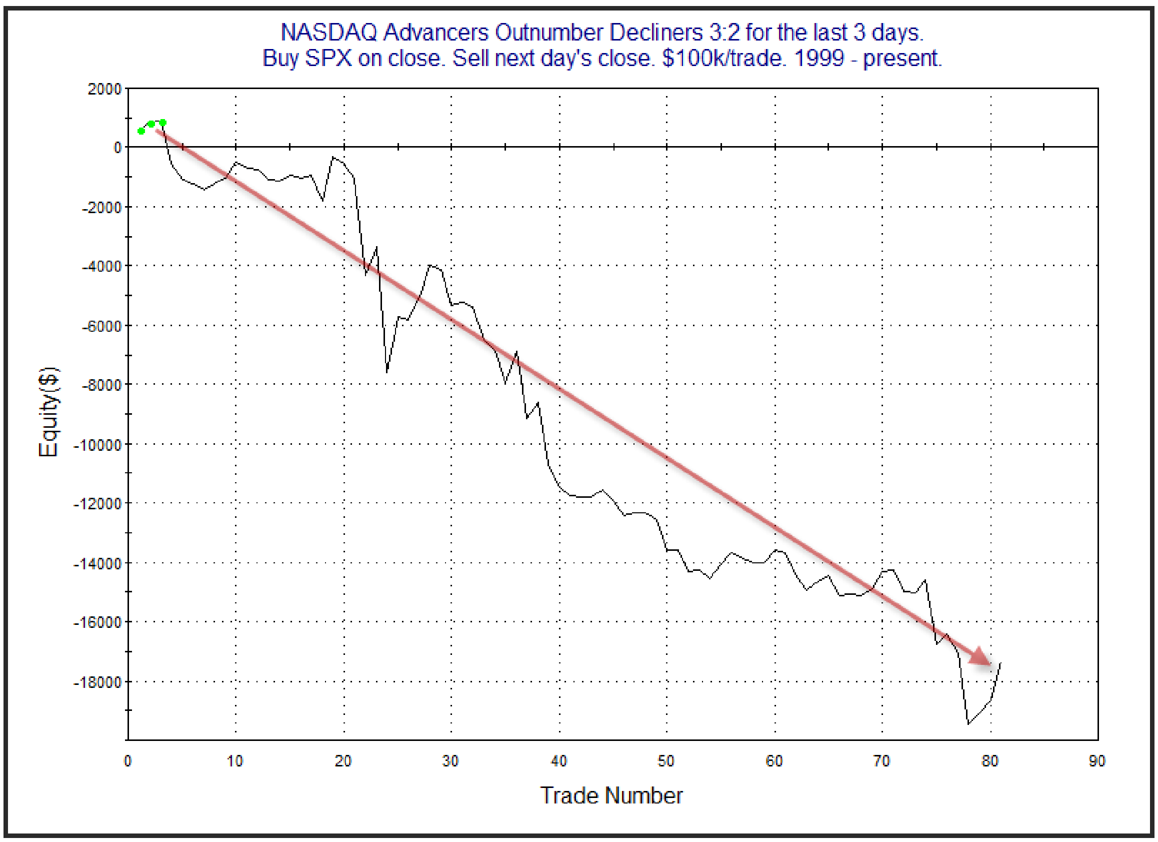
NASDAQ Advancers Outnumber Decliners 3:2 for the last 3 days.
Buy SPX on close. Sell next day's close. $100k/trade. 1999 - present.

TradeStation Performance Summary Expand

All Trades

Total Net Profit	($17,348.40)	Profit Factor	0.48
Gross Profit	$15,864.63	Gross Loss	($33,213.03)
Total Number of Trades	81	Percent Profitable	43.21%
Winning Trades	35	Losing Trades	46
Even Trades	0		
Avg. Trade Net Profit	($214.18)	Ratio Avg. Win:Avg. Loss	0.63
Avg. Winning Trade	$453.28	Avg. Losing Trade	($722.02)
Largest Winning Trade	$1,857.24	Largest Losing Trade	($4,241.94)

The numbers are compelling for the bears. Below is a profit curve.



The strong, long-term downslope is impressive. This study appears worth consideration, and I have again put it on the Active List.

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Lastly, there was some pattern-based bearish evidence to consider. The study below last appeared in the 8/12/11 letter. I have updated the results.

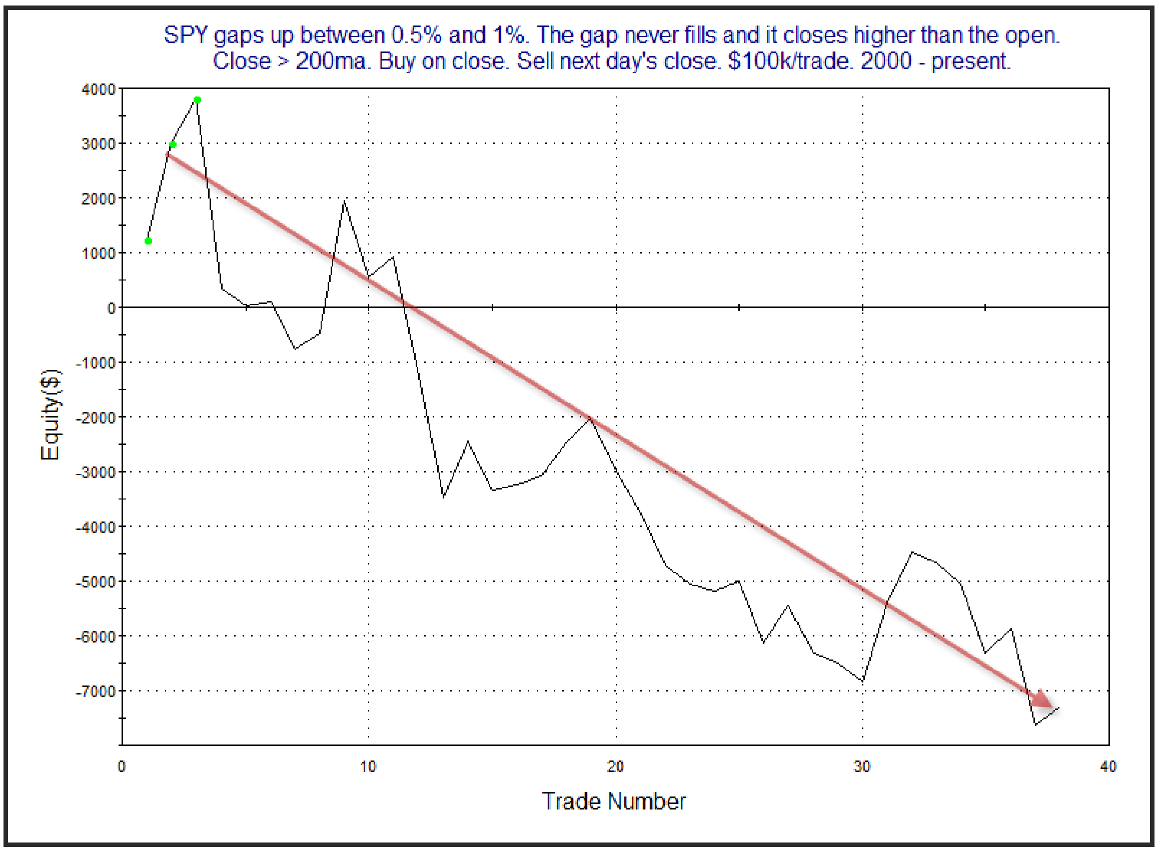
SPY gaps up between 0.5% and 1%. The gap never fills and it closes higher than the open. Close > 200ma. Buy on close. Sell next day's close. $100k/trade. 2000 - present.

TradeStation Performance Summary Expand

All Trades

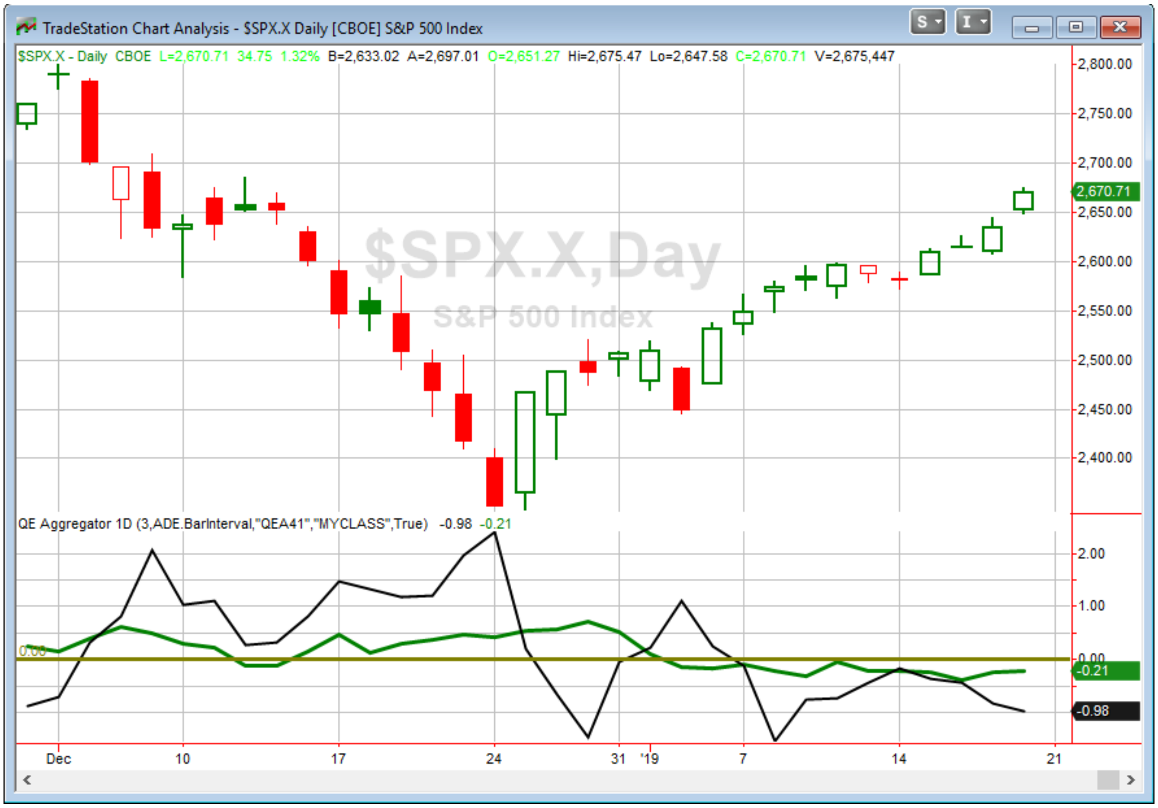
Total Net Profit	($7,290.22)	Profit Factor	0.65
Gross Profit	$13,328.35	Gross Loss	($20,618.57)
Total Number of Trades	38	Percent Profitable	47.37%
Winning Trades	18	Losing Trades	20
Even Trades	0		
Avg. Trade Net Profit	($191.85)	Ratio Avg. Win:Avg. Loss	0.72
Avg. Winning Trade	$740.46	Avg. Losing Trade	($1,030.93)
Largest Winning Trade	$2,416.96	Largest Losing Trade	($3,474.68)

Consistency appeared somewhat weak, which gave me some pause. But take a look at the equity curve.



That is a pretty steady decline, and it has me also factoring in this study when determining my bias.

I have updated the Aggregator chart below.



With tonight's studies considered, the green Aggregator Line held below zero. Negative readings mean net expectations are for downside over the next few days. Meanwhile, the black Differential Line also remained below 0. The negative Differential Line reading means SPX is overbought versus recent expectations. So expectations are negative and SPX is overbought. This is considered a bearish configuration. Bearish configurations are visible on the chart whenever both lines close below zero. Therefore, the Aggregator signal stayed short at the close.

With the current list of active studies, expectations are slated to remain bearish on Tuesday. Of course this could change if compelling new bullish evidence emerges. The Differential Pivot will be 2593.49 on Tuesday. That is 2.9% below Friday's close. So SPX will need to close down at least 2.9% on Tuesday in order to turn from overbought to oversold vs expectations. Even in this volatile market, it is unlikely we will see a drop that large. A more likely scenario for working off the overbought condition would be a multi-day pullback or consolidation.

Short-term evidence continues to all show up bearish. The market is overbought, breadth is short-term overdone, and gapping patterns are all suggesting a pullback. Bearish evidence continues to mount, and the market continues to rise against it. This leaves us in basically the same position as the last few nights. The bearish evidence has not mattered yet. At some point it will. I have a small short position. But with the intermediate-term outlook leaning bullish, this is a counter-trend trade. I generally trade counter-trend more conservatively, and so rather than add more at this point, I will remain lightly positioned to the short side.

Intermediate-term Outlook (2 weeks – 2 months) – updated 1/22– somewhat bullish

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

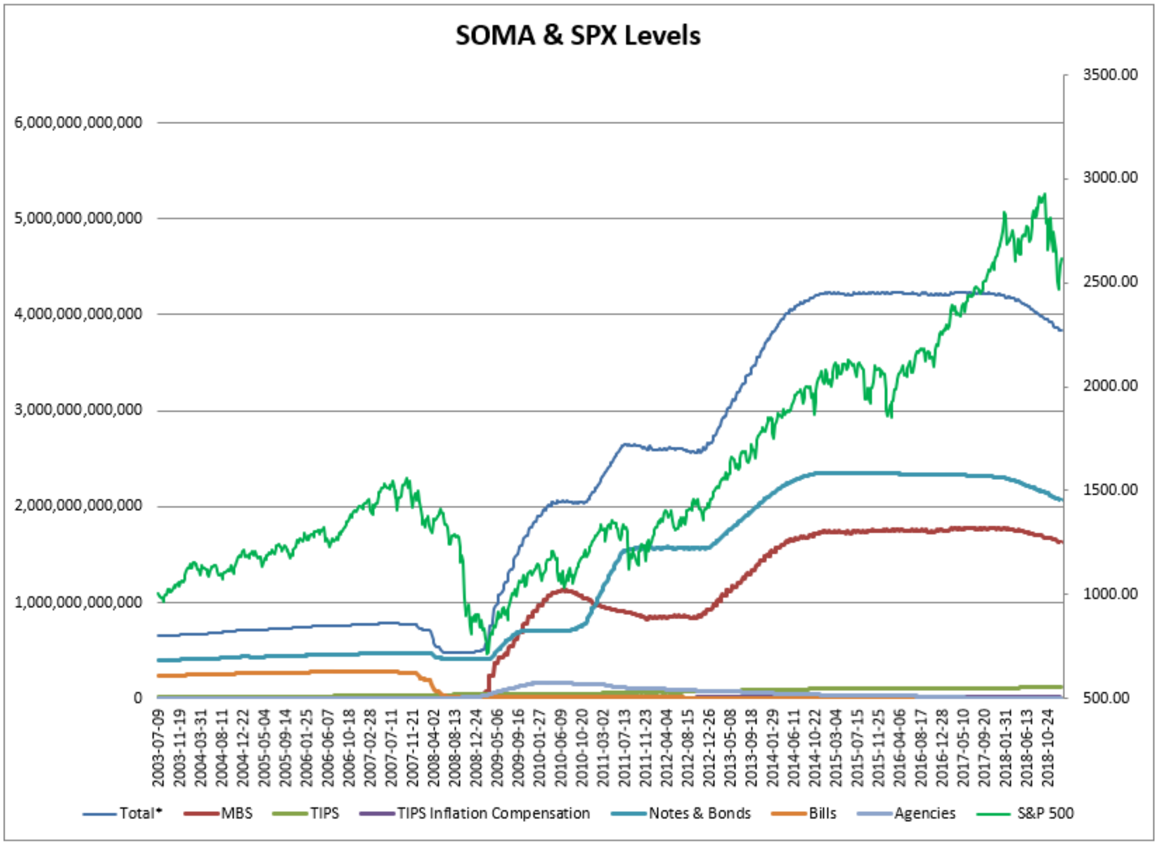
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the Quantifiable Edges Market Timing Course, which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

A persistently overbought market during a poor seasonal week could not thwart the rally this past week. The SPX rose 2.9%, the NASDAQ closed up 2.7%, and the Russell 2000 climbed 2.4%. There were not any new and compelling studies that emerged with intermediate-term implications.

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 01/09/2019

DOMESTIC SECURITIES HOLDINGS AS OF
January 16, 2019

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)	2,064,760,611.5
US Treasury Floating Rate Notes (FRN)	18,825,874.1
US Treasury Inflation-Protected Securities (TIPS)*	114,768,909.8
Federal Agency Securities**	2,409,000.0
Agency Mortgage-Backed Securities***	1,632,728,750.9
Total SOMA Holdings	3,833,493,146.3
Change From Prior Week	-6,170,412.5

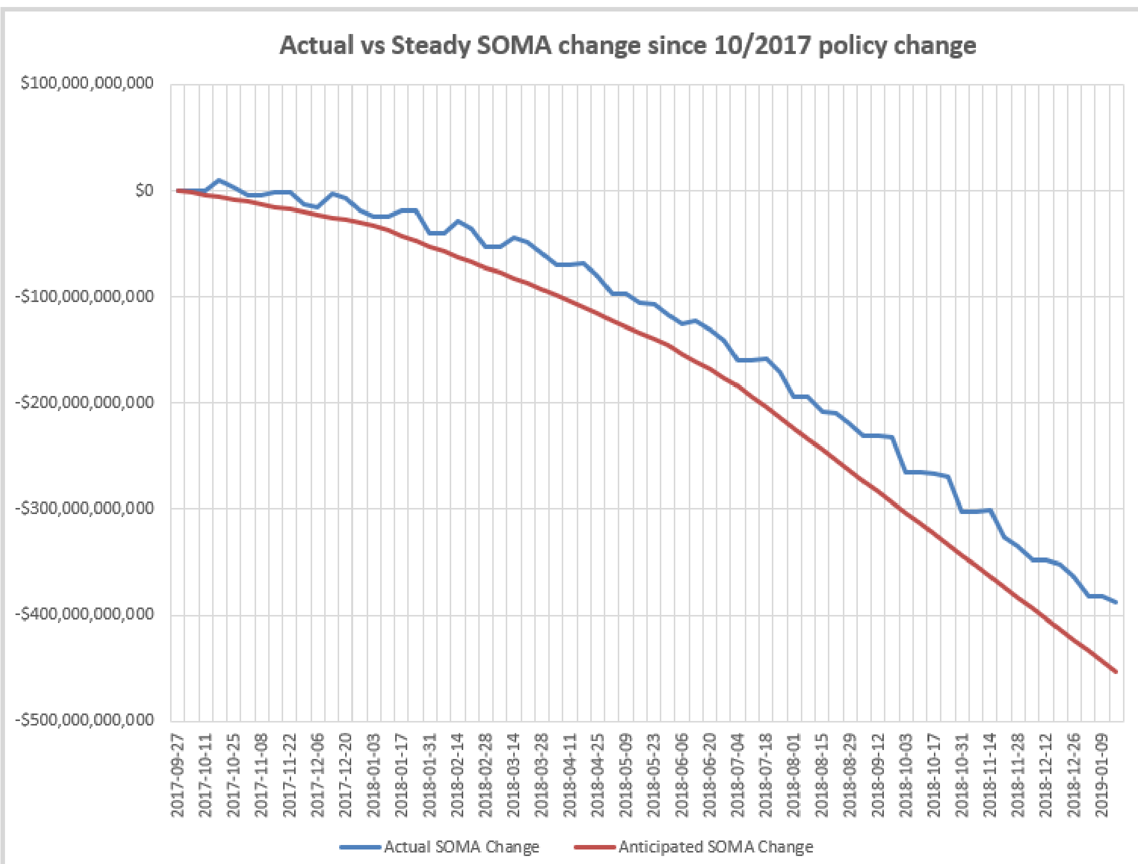
*Does not reflect inflation compensation of 21,863,194.7

**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.

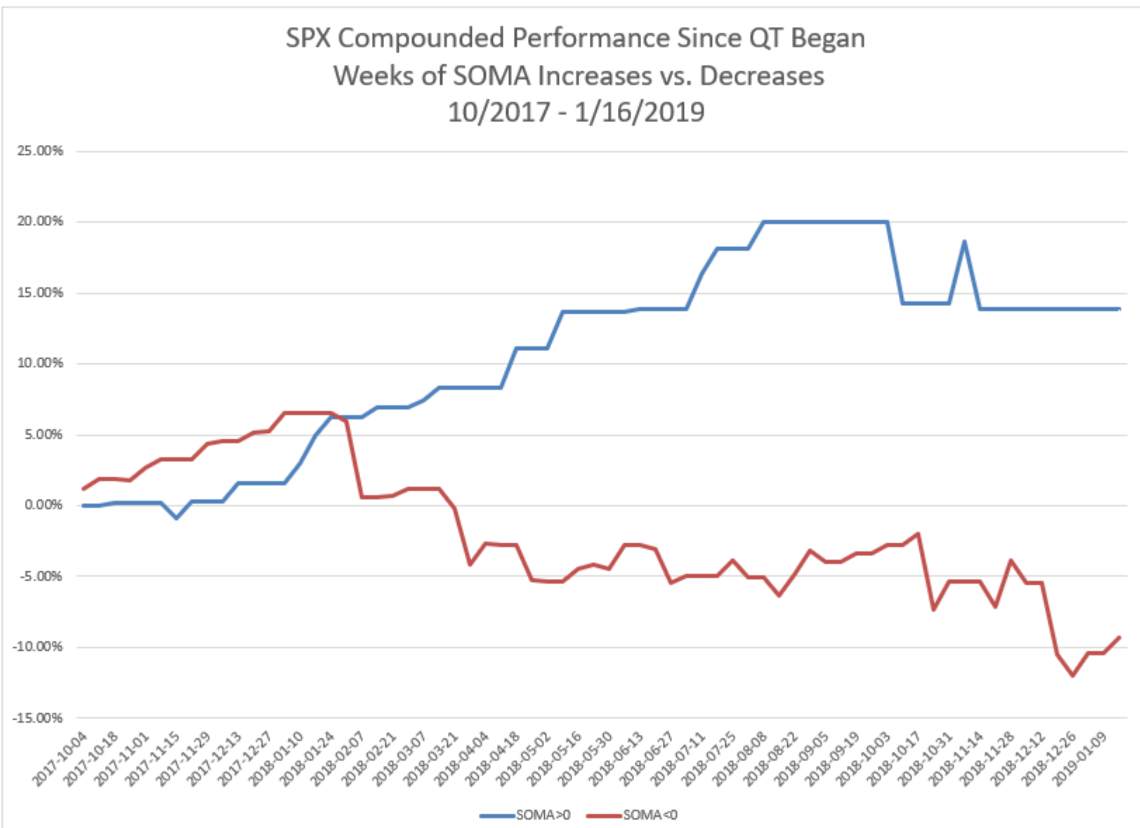
Data posted on 01/17/2019 4:30pm.

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



The Fed's SOMA this past week (Wednesday to Wednesday) declined about $6.2 billion. We were expecting mild Quantitative Tightening (QT) this past week. This is a little stronger than expected, but still not terribly strong, and in the proper direction. Meanwhile, the SPX gained 1.2% for the week ending 1/16. That is a good sized gain, especially for a week where there was QT. The "Actual vs Steady" chart shows that the $6.2 billion decline is a mild decline for a week with the 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 16 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 9.4%. 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 12/26/2018

DOMESTIC SECURITIES HOLDINGS AS OF

January 2, 2019

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]
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%		

Notable here is that the next set of expirations is on 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.

Looking at this week, ending on Wed. the 23rd, SOMA change is again not completely obvious. May ended on the 23rd, and that saw a mild decline in the SOMA. Same with 10/24/18 and 8/22/18. But 1/24/18 and 11/22/17 saw small increases. I think there is a good chance that the SOMA declines on the week ending 1/23, but I expect it to be mild.

The next week, ending on the 30th, I expect to see a more substantial SOMA decline. And of course the week after that as well since we will see the treasury expirations on the 31st.

Intermediate-term indications are continuing to lean bullish. All 3 Market Timing Course signals are long. And the strong breadth thrust off the bottom has generated terrific upside momentum. Our Zweig Breadth Thrust and 3x 70% Up Issues studies both suggest the rally has staying power. QT remains the primary concern for the intermediate-term. I am again somewhat bullish, which means I will be more conservative with short trades than with long trades.

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
SPY(s)(1/4)	1/9/2019	$257.56	$266.46	-3.46%		Aggregator

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