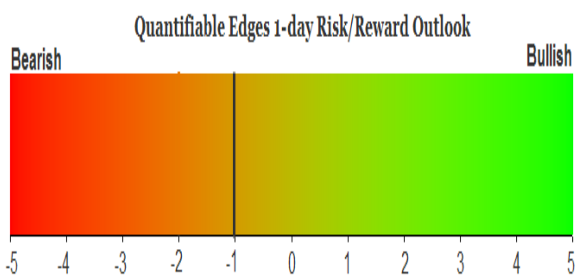
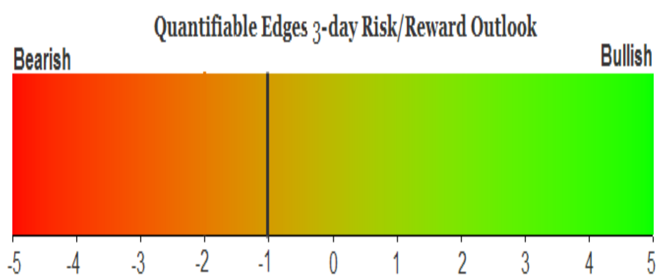
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 8, 2019 Volume 12 Issue 129

Market Overview





Signals Overview

Aggregator	CBI Reading
Short	0

Tonight's Research Points

- 5 days higher to a 50-day high rarely sees the move up end abruptly.
- Unfilled gaps down from intermediate-term high will frequently be followed by more selling.

Short-term Outlook

The Bottom Line

The Aggregator is suggesting a slight bearish edge. But I am not terribly enthused by the potential reward/risk.

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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						
July 8, 2019	Unfill up 20-high the unfill down	1-3 days	Bearish			
July 8, 2019	5-up to 50-high and then 1 down	1-4 days	Bullish			
Active - Long Term						
July 8, 2019	5-up to 50-high and then 1 down	1-10 days	Bullish			
July 8, 2019	NASDAQ Leading	int term	Bullish			
June 21, 2019	SPX RSI2 crosses over 99.	1-15 days	Bullish			
April 2, 2019	Golden Cross	int term	Bullish			
October 1, 2018	Quantitative Tightening	int term	Bearish			

The Evidence

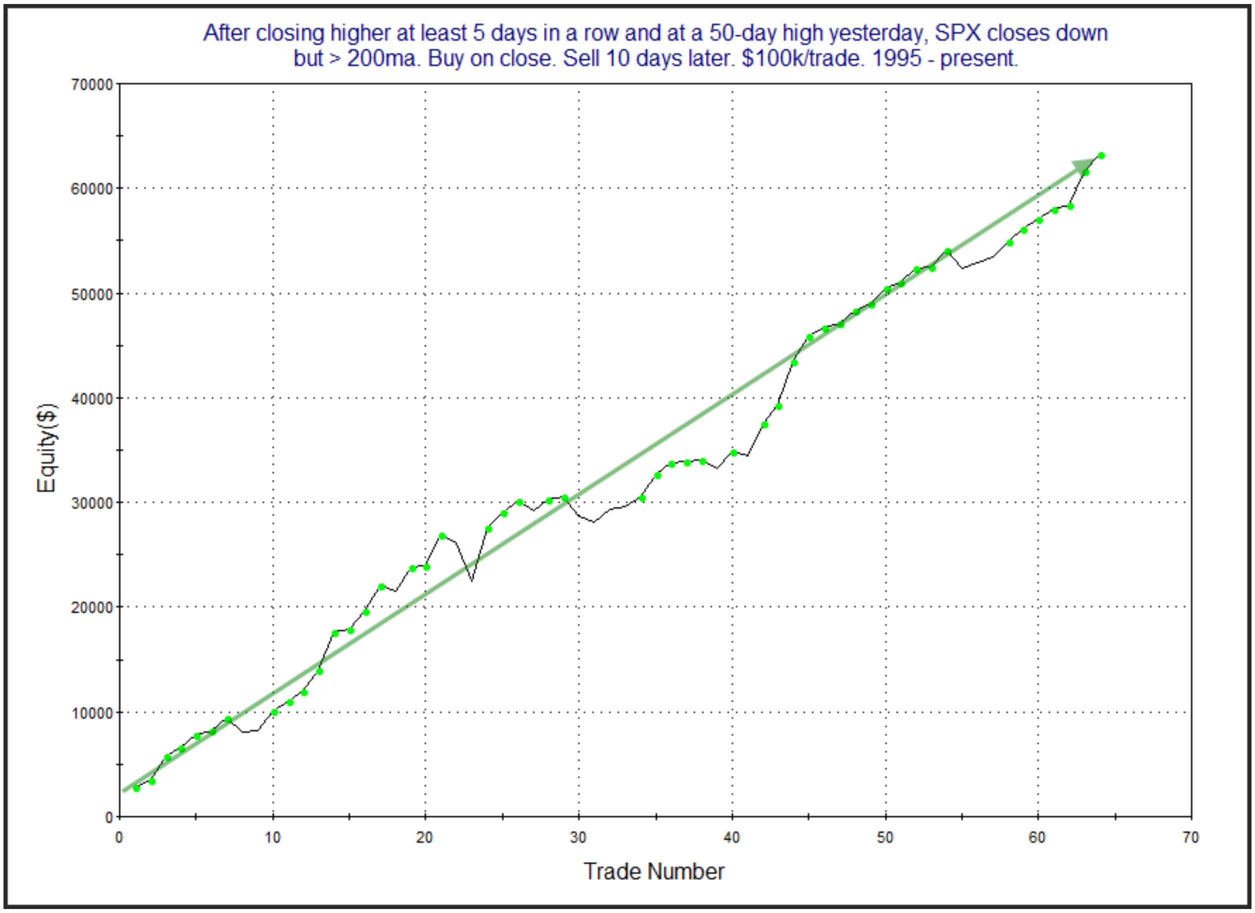
Friday started very weak but finished mixed. The SPX lost 0.2%, the NASDAQ fell 0.1%, and the Russell 2000 gained 0.2%. Breadth was also mixed as the NYSE Up Issues % was 48% and the Up Volume % came in at 58%. NYSE volume rose from Wednesday's level but was still very light.

One compelling study that triggered tonight suggested the recent persistent upmove is unlikely to abruptly end. (This is a theme we have seen many times over the years.) It considers what happens after the market moves up at least 5 days in a row to a 50-day high, and then pulls back. It was last seen in the 4/10/19 Letter. I have updated the stats in the table below.

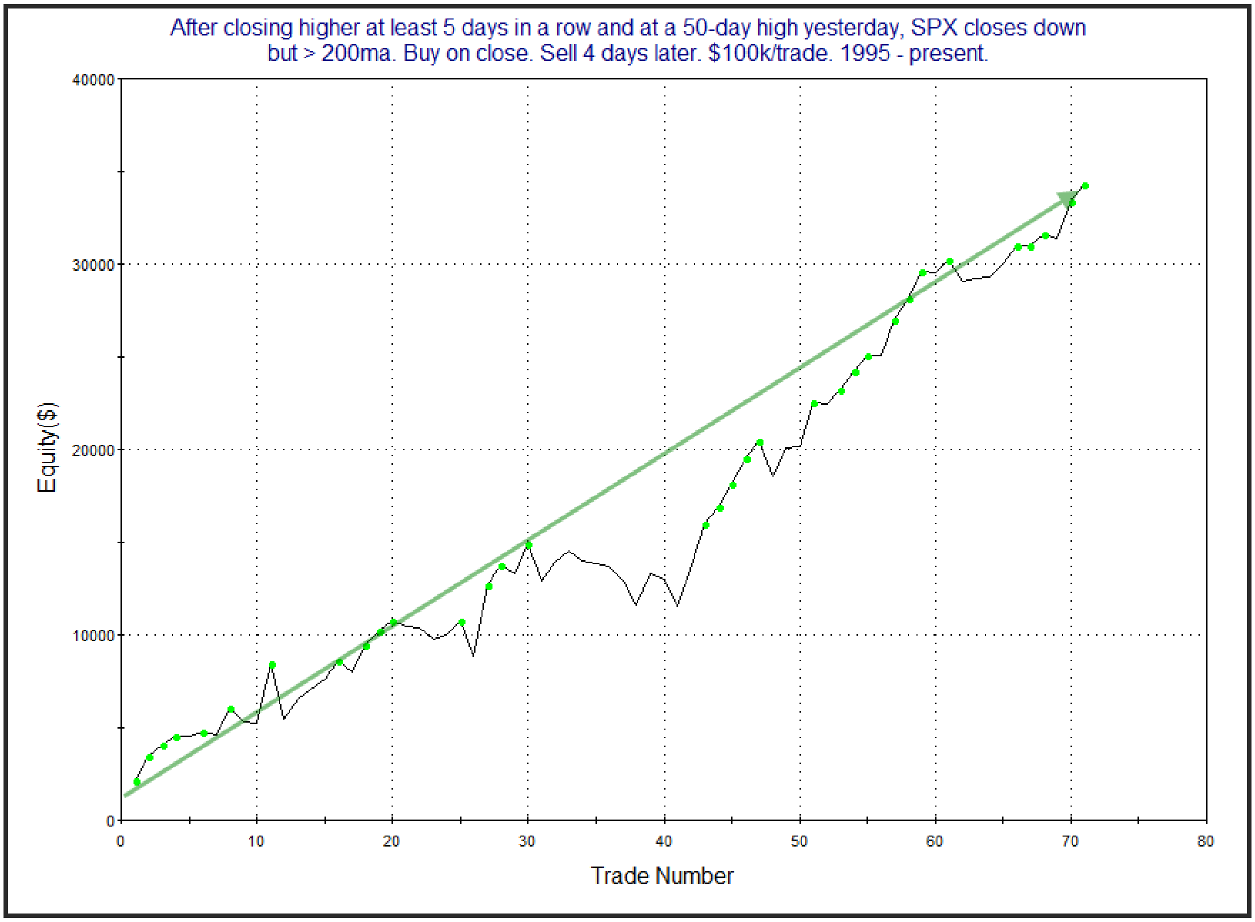
After closing higher at least 5 days in a row and at a 50-day high yesterday, SPX closes down but > 200ma. Buy on close. Sell X days later. $100k/trade. 1995 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Max Winning Trade	All: Max Losing Trade	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	63,336.16	64	54	10	84.38	5,131.35	-3,672.90	1,412.26	-1,292.59	1.09	5.90	989.63
9	62,064.82	67	55	12	82.09	5,023.20	-4,151.40	1,410.32	-1,291.89	1.09	5.00	926.34
8	53,775.55	68	49	19	72.06	4,878.08	-4,874.10	1,562.77	-1,200.01	1.30	3.36	790.82
7	41,861.59	69	48	21	69.57	3,874.76	-3,912.48	1,405.07	-1,218.18	1.15	2.64	606.69
6	40,398.79	71	50	21	70.42	4,307.20	-3,637.71	1,275.06	-1,112.10	1.15	2.73	569.00
5	31,968.01	71	46	25	64.79	4,252.50	-2,466.75	1,119.75	-781.62	1.43	2.64	450.25
4	34,303.95	71	46	25	64.79	3,843.00	-3,003.39	1,141.88	-728.90	1.57	2.88	483.15
3	21,648.85	71	46	25	64.79	2,472.85	-1,992.34	868.60	-732.26	1.19	2.18	304.91
2	19,897.92	71	49	22	69.01	2,437.50	-2,614.95	732.98	-728.10	1.01	2.24	280.25
1	11,809.62	71	47	23	66.20	1,751.19	-1,744.10	496.04	-500.18	0.99	2.03	166.33

We see here a decent edge that becomes stronger and more consistent as you look out over the next several days. The 9-10 day time frame shows exceptional stats. The 2-4 day timeframe suggests a short-term boost is also likely. Let's take a look below at both the 10-day and 4-day exit profit curves. First, the 10 day.



The strong upslope appears to confirm the bullish edge. Next let's look at the 4-day curve.

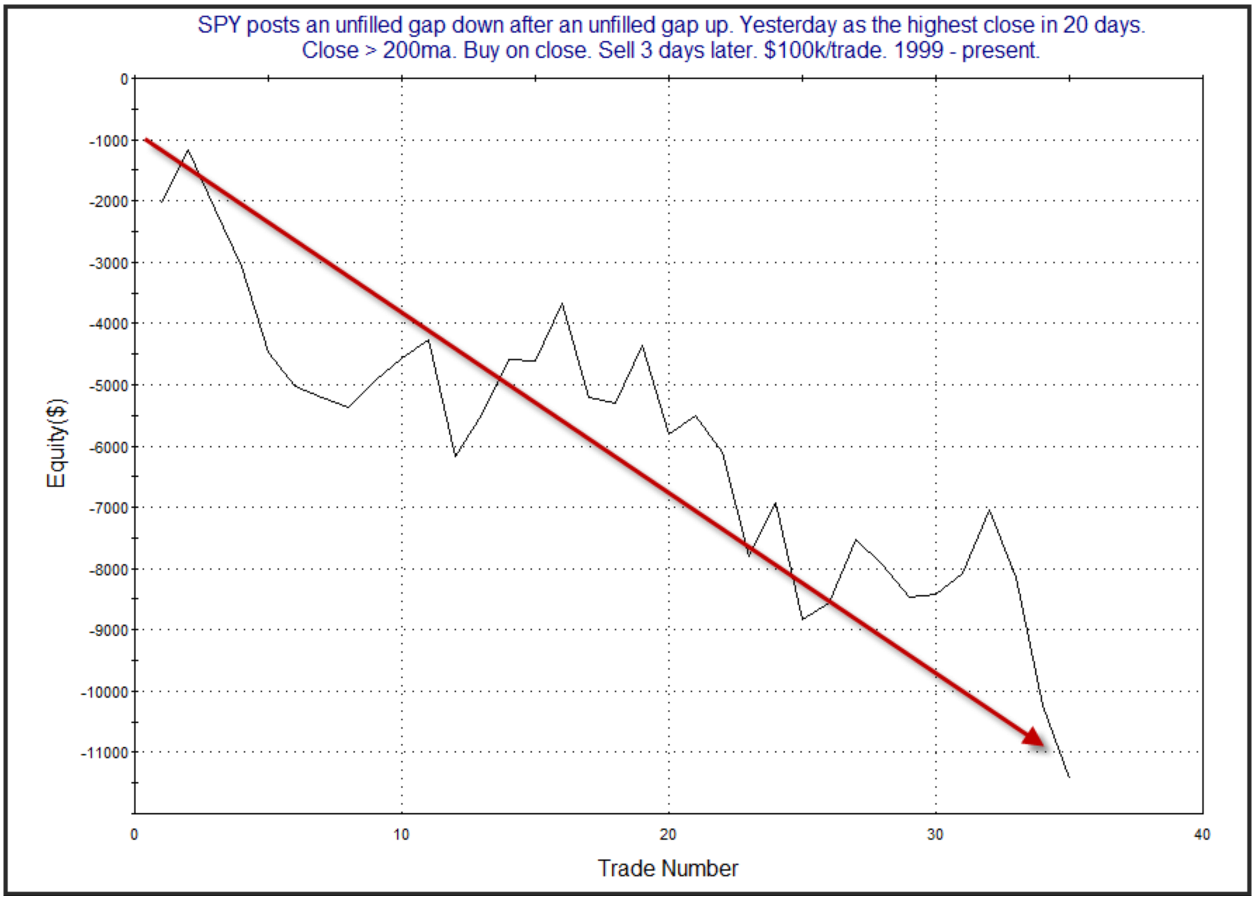


Results are choppier. But even with more whipsaws this one appears worthy of consideration. I have included this study on both the short-term and intermediate-term active lists.

One potential issue with Friday's decline is that it included an unfilled gap down. Generally, an unfilled gap down from a high has more trouble quickly rebounding that a decline that does not include an unfilled gap. Unfilled gaps from high levels will often trap some recent bulls that bought the day before. The unfilled gap meant they were not given an opportunity to exit their positions with a profit. And if they are feeling anxious right now, that could lead to some more selling the following days. At the very least, they are more unlikely to be let off the hook as easily as if there was not an unfilled gap. You can see this exemplified in the study below, which was last seen in the 1/11/18 letter.

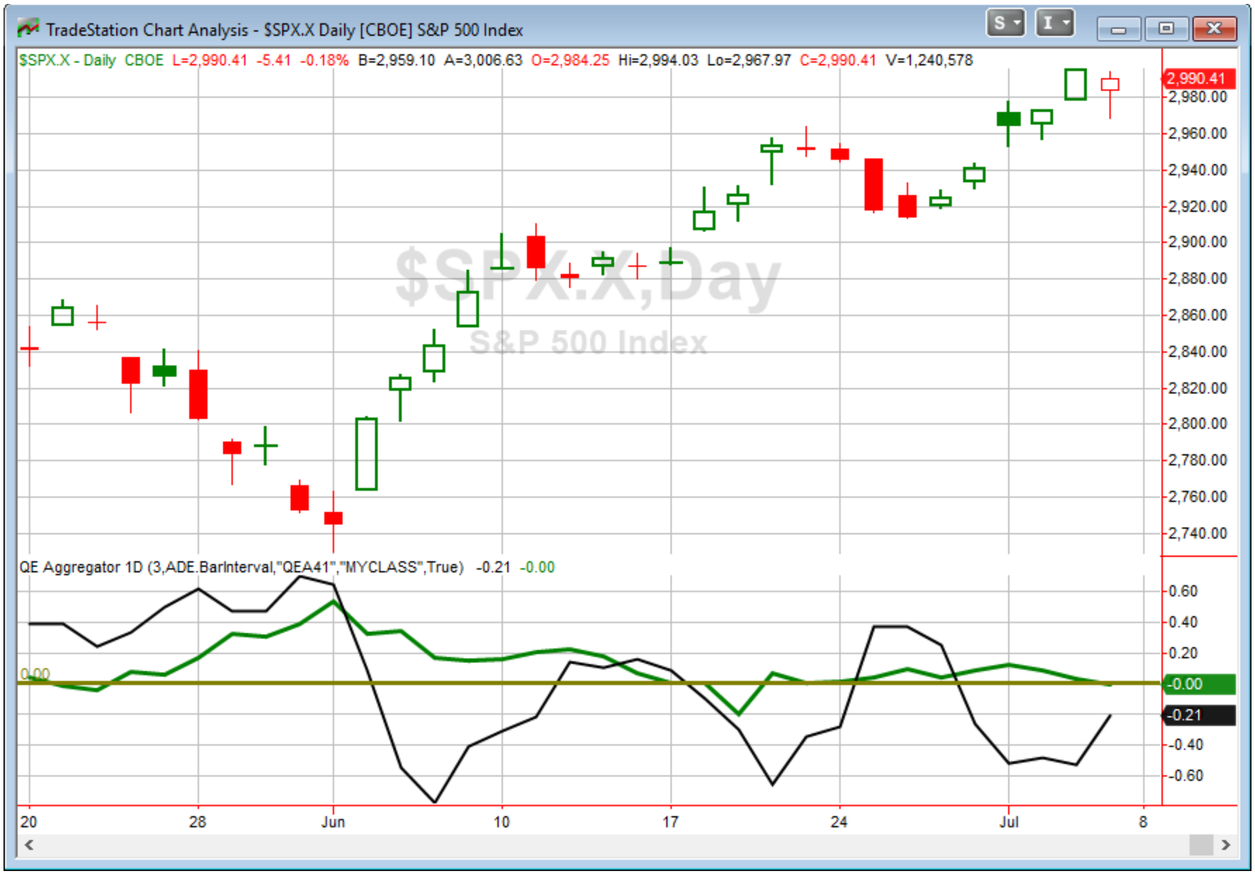
SPY posts an unfilled gap down after an unfilled gap up. Yesterday as the highest close in 20 days. Close > 200ma. Buy on close. Sell X days later. $100k/trade. 1999 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Max Winning Trade	All: Max Losing Trade	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-18,092.47	35	16	19	45.71	1,827.28	-7,283.25	821.97	-1,644.42	0.50	0.42	-516.93
4	-13,893.13	35	15	20	42.86	1,998.36	-3,746.95	785.30	-1,283.63	0.61	0.46	-396.95
3	-11,436.47	35	15	20	42.86	1,044.24	-2,100.56	622.73	-1,038.87	0.60	0.45	-326.76
2	-7,945.77	36	14	22	38.89	1,383.20	-2,232.00	562.66	-719.23	0.78	0.50	-220.72
1	-6,139.87	36	15	21	41.67	1,008.68	-1,807.92	438.20	-605.38	0.72	0.52	-170.55

The numbers suggest a bit of a downside edge. The 3-day profit curve can be seen below.



While the curve is choppy, it has persisted downwards. This serves as confirmation of the downside edge, and suggests we could see further selling over the next few days. So the short-term Active List received one bullish and one bearish study tonight.

I have updated the Aggregator chart below.



With tonight's evidence considered, the green Aggregator Line dipped just barely below zero. Negative readings mean net expectations are for downside 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 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 turned short at the close.

Based on the current Active Studies list, expectations are slated to flip to mildly bullish on Monday. Of course this could change if compelling new bearish evidence emerges. The Differential Pivot will be 2981.18 on Monday. That is 0.3% below Friday's close. Therefore SPX would need to close down at least 0.3% on Monday in order to flip from overbought to oversold versus expectations.

While the Aggregator formation is bearish, it is a very weak bearish signal. First of all, the bearish evidence is light. And with evidence mixed, it is also set to flip to bullish in just 1 day. There also is not a lot of room to the downside before SPX would flip from overbought to oversold. And also well worth considering is the fact that short trade would be counter-trend at this point. As I discuss in the next section, a bullish intermediate-term outlook means I will be extra-cautious with potential short trades. This includes "passing" on borderline setups like we see now. I will continue to wait for a more compelling reward/risk scenario to emerge before taking on new index positions.

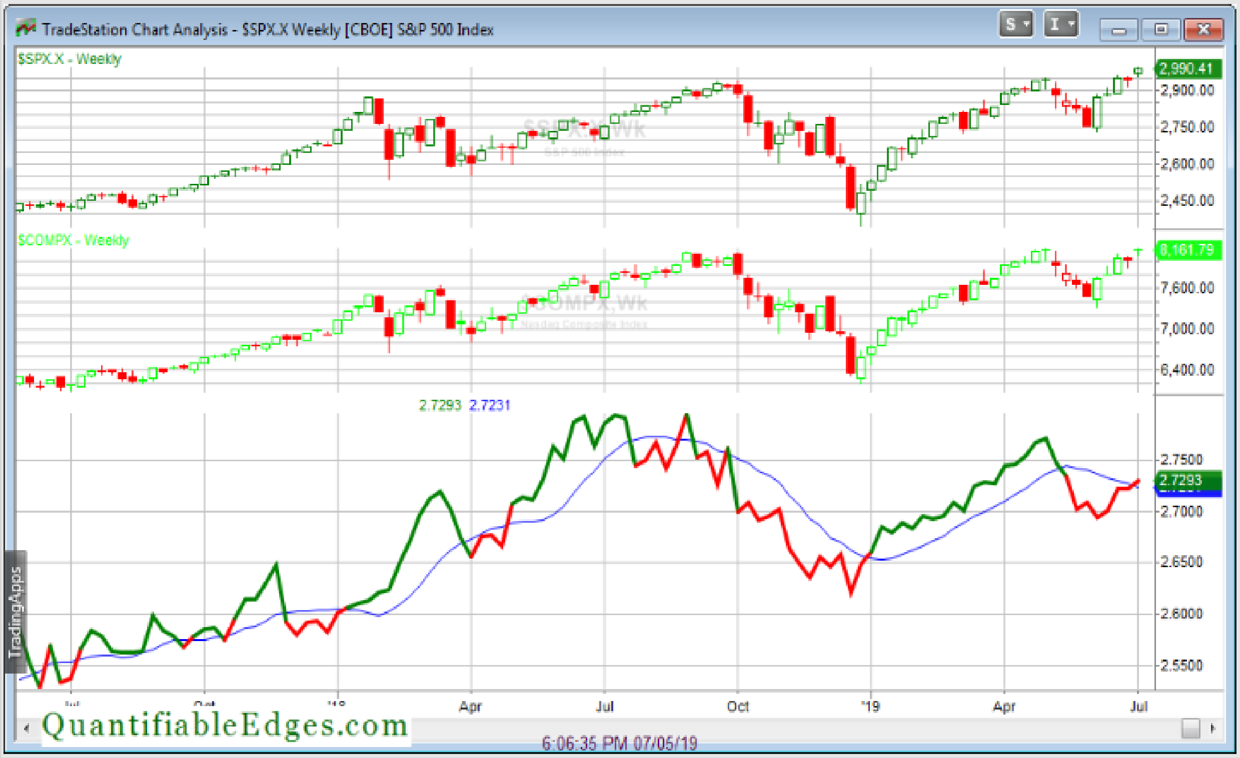
Intermediate-term Outlook (2 weeks – 2 months) – updated 7/8– somewhat bullish

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 saw Combo System #3 turn Long to match the other two.*

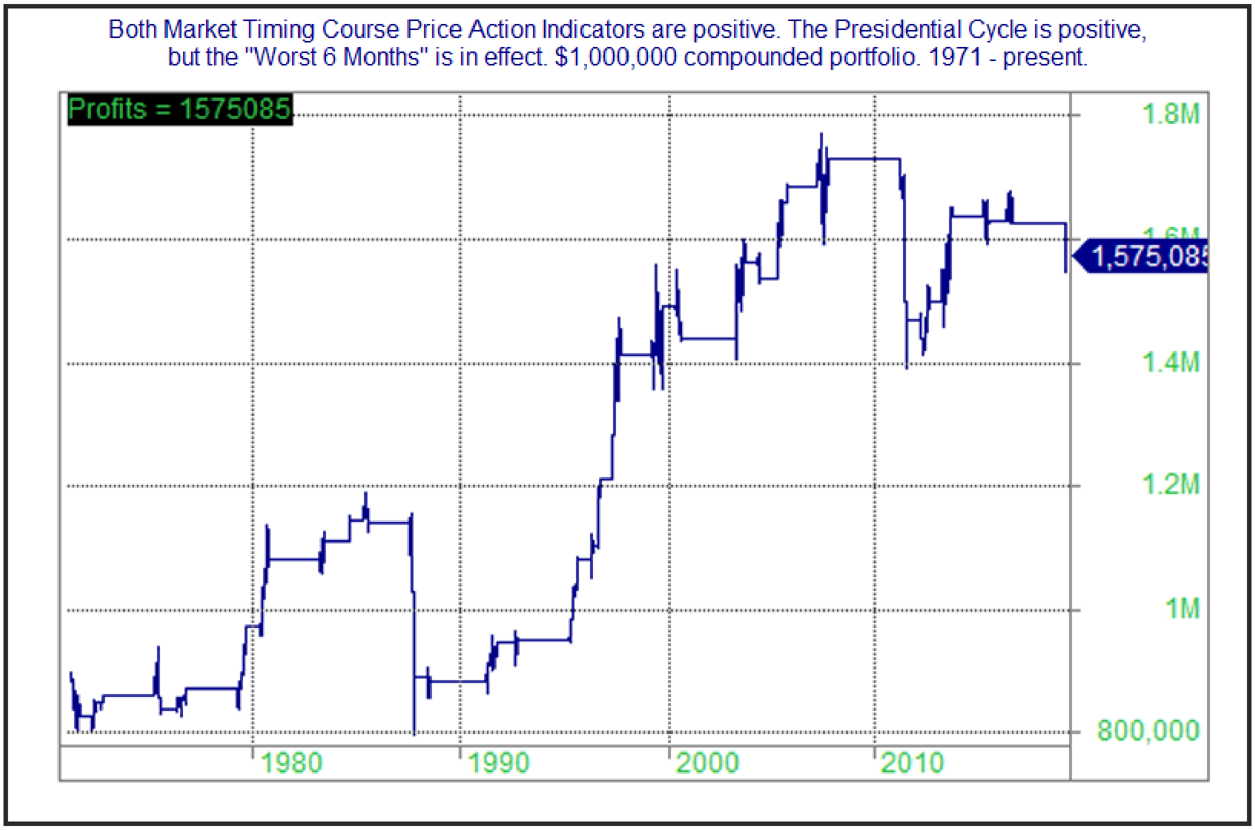
This past week was a strong one for the indices. The SPX gained 1.7%, the NASDAQ rose 1.9%, and the Russell 2000 climbed 0.6%. The Dow, SPX and NASDAQ all made new all-time highs during the week. So there is no doubt the market remains in an uptrend for the time being. There was one study I noted above in the short-term section that also had intermediate-term implications. It is also notable that the NASDAQ took back leadership from the SPX based on our NASDAQ/SPX Relative Strength indicator. This can be seen in the chart below, copied from the website:

NASDAQ/S&P 500 Relative Strength Weekly



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 2281.08 points when the NASDAQ has been leading versus 606.51 points when the NASDAQ has lagged. The difference for the NASDAQ has been even more dramatic, with the point gains being 7105.09 vs. just 948.32. 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) favorable Presidential Cycle, and 4) "Worst" 6 months in effect. Below are updated stats showing SPX performance during this alignment.

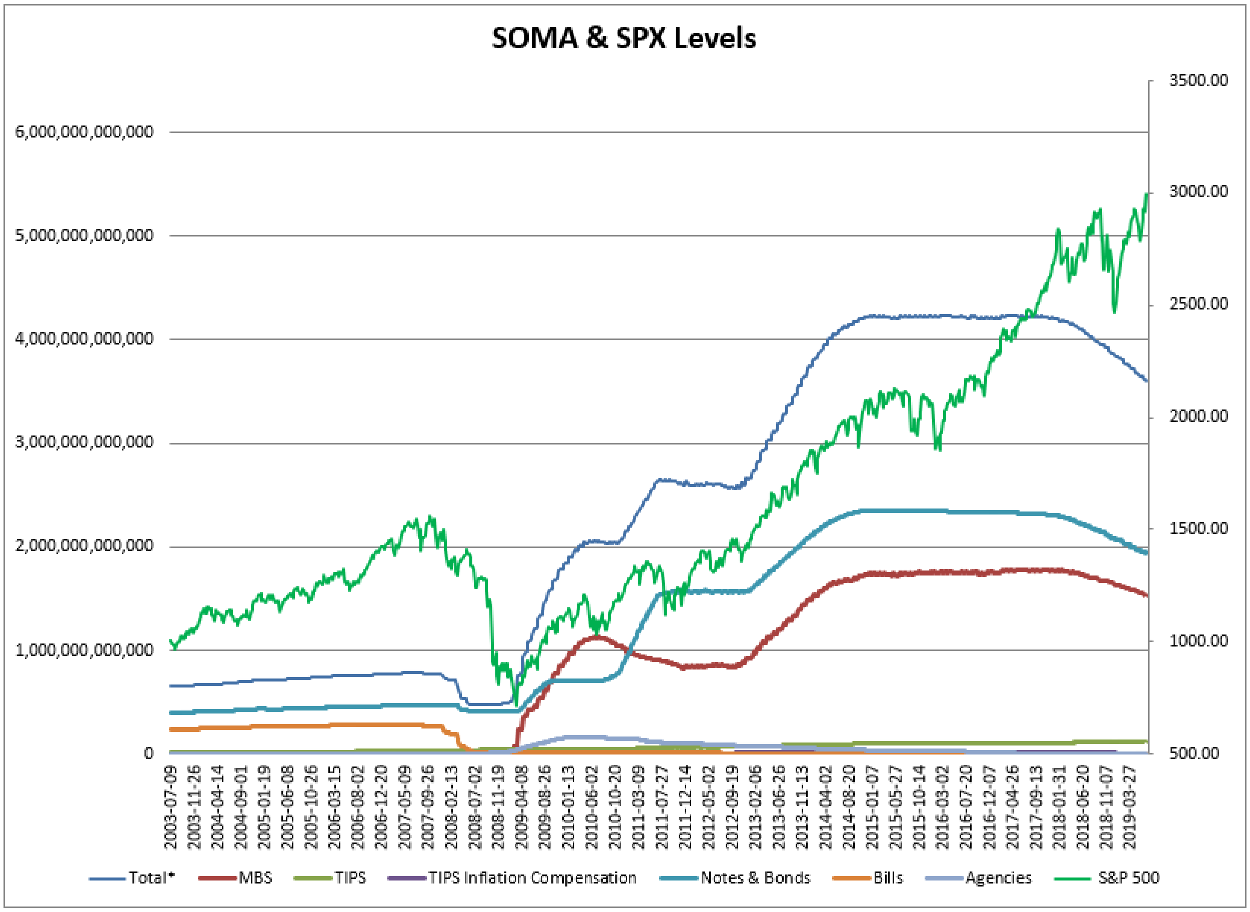


We see here that similar formations have seen gains in the past. It is notable though that this chart has had some sizable drawdowns along the way, and it is not exactly a smooth ride higher. So perhaps the setup could be viewed as bullish, or perhaps your interpretation would be more neutral. In any 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 now positive, all 3 "Combo" systems we track are now "Long".

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. 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 06/26/2019

DOMESTIC SECURITIES HOLDINGS AS OF

July 3, 2019

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

Security Type	Total (in Thousands)
US Treasury Bills (T-Bills)	5,000.0
US Treasury Notes and Bonds (Notes/Bonds)	1,940,450,432.5
US Treasury Floating Rate Notes (FRN)	14,819,524.4
US Treasury Inflation-Protected Securities (TIPS)*	116,516,485.4
Federal Agency Securities**	2,347,000.0
Agency Mortgage-Backed Securities***	1,532,726,161.0
Total SOMA Holdings	3,606,864,603.3
Change From Prior Week	-15,000,001.0

*Does not reflect inflation compensation of 23,601,359.1

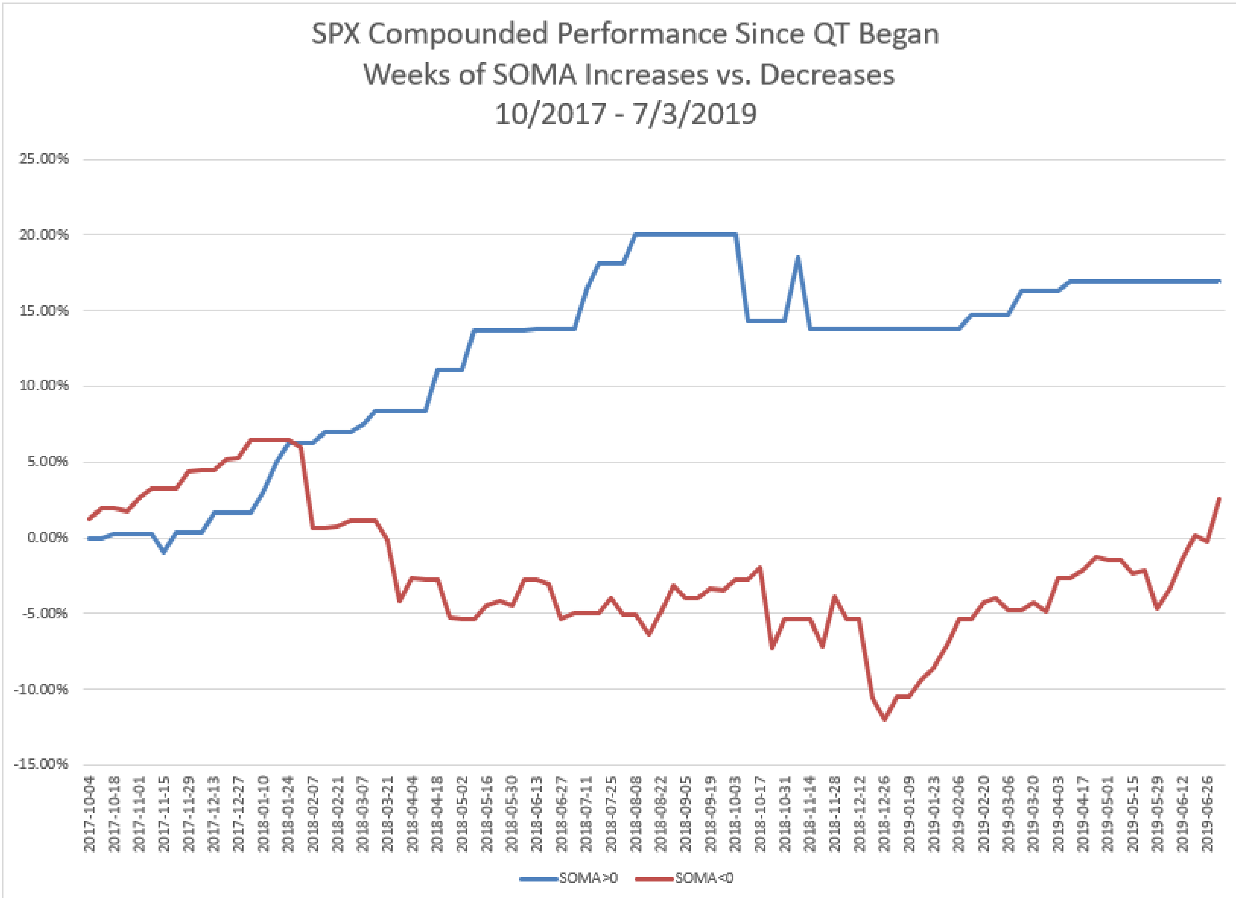
**Fannie Mae, Freddie Mac and Federal Home Loan Bank

***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 07/05/2019 4:30pm.

The Fed's SOMA this past week (Wednesday to Wednesday) fell $15 billion. That is a large contraction. Meanwhile the SPX rallied an impressive 2.8% over the same period. That is a big amount, and especially large for a SOMA contraction 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.



You can see here the sharp contrast in expansion weeks versus contraction weeks over the last year and a half. Despite some brief struggles last September and October, expansion weeks (blue line) have seen strong gains. Meanwhile, weeks with QT (red line) have struggled, though the chart has recovered quite a bit since last Christmas. Since October 2017 the blue "expansion week" strategy would have posted a 17.0% gain while the red "contraction week" strategy would have gained 2.6%. That is a substantial difference in performance. So how might the next few weeks of Quantitative Tightening (QT) play out? Let's first look at the T-Note and T-Bond Maturity Table below, from the Fed's website.

« As of 06/26/2019

DOMESTIC SECURITIES HOLDINGS AS OF
July 3, 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]
7/15/19	912828S43	0.750	1,563,173.6	6.11%		
7/31/19	912828TH3	0.875	14,516,000.0	50.06%		
7/31/19	9128282K5	1.375	2,643,540.3	9.23%		
7/31/19	912828WW6	1.625	623,370.1	1.78%		
8/15/19	912810ED6	8.125	13,258,100.0	70.00%		
8/15/19	9128282B5	0.750	2,458,280.2	9.29%		
8/15/19	912828LJ7	3.625	39,098,027.1	58.57%		

We see here a small number of treasuries are set to expire on 7/15/19. The next batch of expirations will occur at the end of the month.

Weeks where there are no treasuries expiring, any QT 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.

This current week, which runs through Wednesday, 7/10 is unlikely to see any QT. In fact, there appears to be a good chance that there will be a small rise, which could serve as a breeze at the bulls backs. The week after that the small treasury expiration basically ensures there will be some Quantitative Tightening to deal with.

Intermediate-term evidence appears favorable. The momentum study featured in the short-term section also shows strong 10-day results. And the NASDAQ taking a leading position should be viewed as a positive as well. With the indices hitting new highs this past week, the bulls also certainly have the trend on their side. The current QT policy remains a concern, though it is only going to last a few months longer. And the Fed's more dovish tone in 2019 certainly seems to have aided the market. I like the bull case. So I'll be extra cautious when considering short trades, and more aggressive with long positions with this in mind.

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

None