

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 6, 2019

Volume 13 Issue 3

## Market Overview



## Signals Overview

Aggregator	CBI Reading
Short	1

## Tonight's Research Points

- Coming from an intermediate-term high, an unfilled gap down after an unfilled gap up appears to be somewhat bearish.
- Intermediate-term evidence continues to point higher.

## *Short-term Outlook*

### *The Bottom Line*

Evidence suggests a pullback over the next few days. But this would be a counter-trend move and SPX could easily turn from short-term overbought to oversold vs expectations on Monday. The short-term edge does not appear substantial or compelling.

*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
<b>Active - Short Term</b>						
January 6, 2020	Unfill gp dn after unfill to to 20-high	1-4 days	Bearish			
January 3, 2020	SPX up on 1st day of year	1-2 days	Bullish			
<b>Active - Long Term</b>						
December 31, 2020	1st 5-day low > 10ma	1-10 days	Bullish	2.10%	-1.35%	-2.60%
November 11, 2019	"not QE"	int term	Bullish			
November 5, 2019	SPX 50-day %b > 100	1-50 days	Bullish	4.90%	-4.20%	-7.90%
November 4, 2019	Presidential cycle + Best 6 mos bullish	6 months	Bullish			
October 28, 2019	NASDAQ Leading	int term	Bullish			
April 2, 2019	Golden Cross	int term	Bullish			

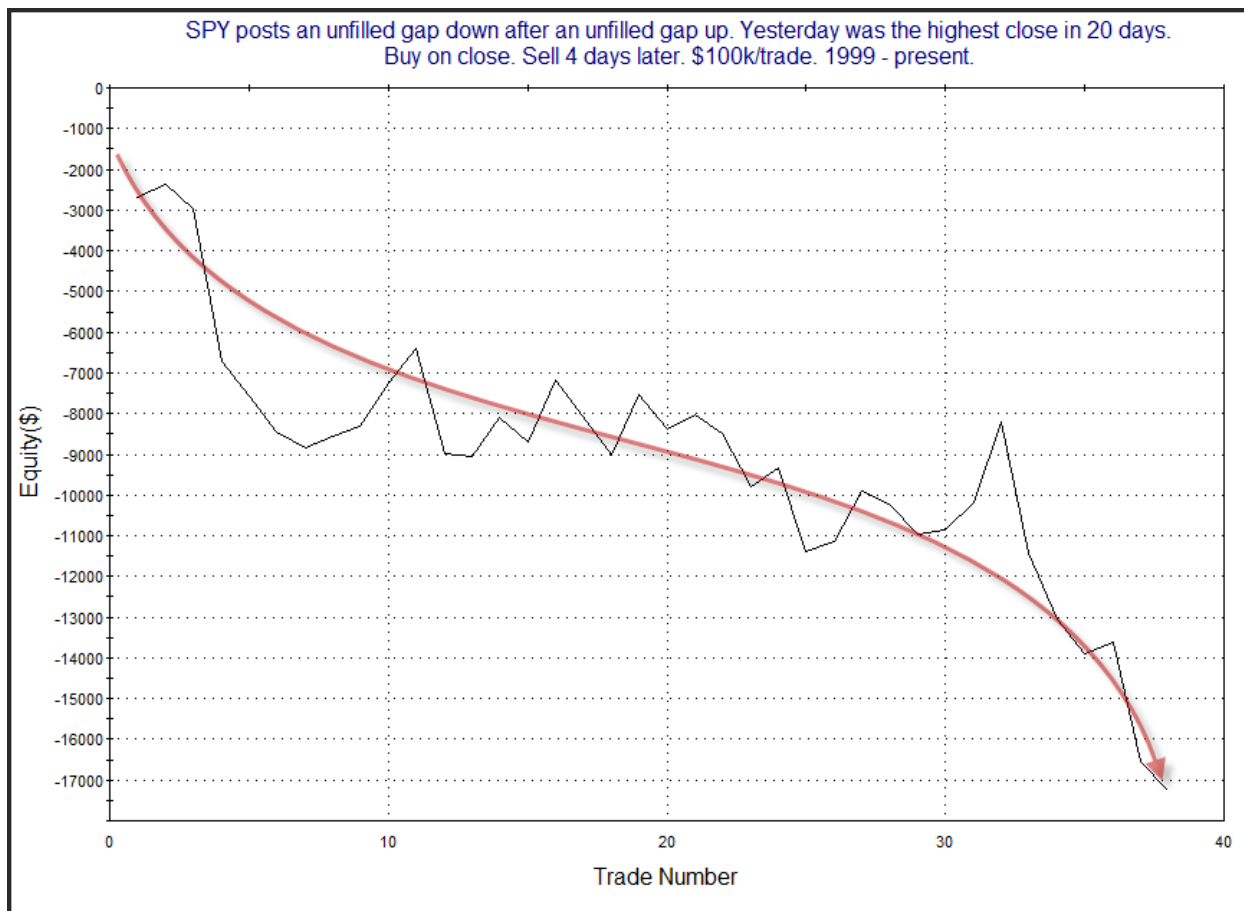
**The Evidence**

Conflict with Iran, and fear of further escalation sparked some selling in the market on Friday. The SPX fell 0.7%, NASDAQ lost 0.8% and Russell 2000 declined 0.35%. Breadth was negative as the NYSE Up Issues % was 48% and the Up Volume % came in at 38%. NYSE volume rose some from Thursday's level.

There was some bearish evidence that emerged Friday based on price action. This study below considers SPY performance after posting an unfilled gap down from a high level immediately after an unfilled gap up. It was last shown in the 12/2/19 Subscriber Letter. Below are updated results.

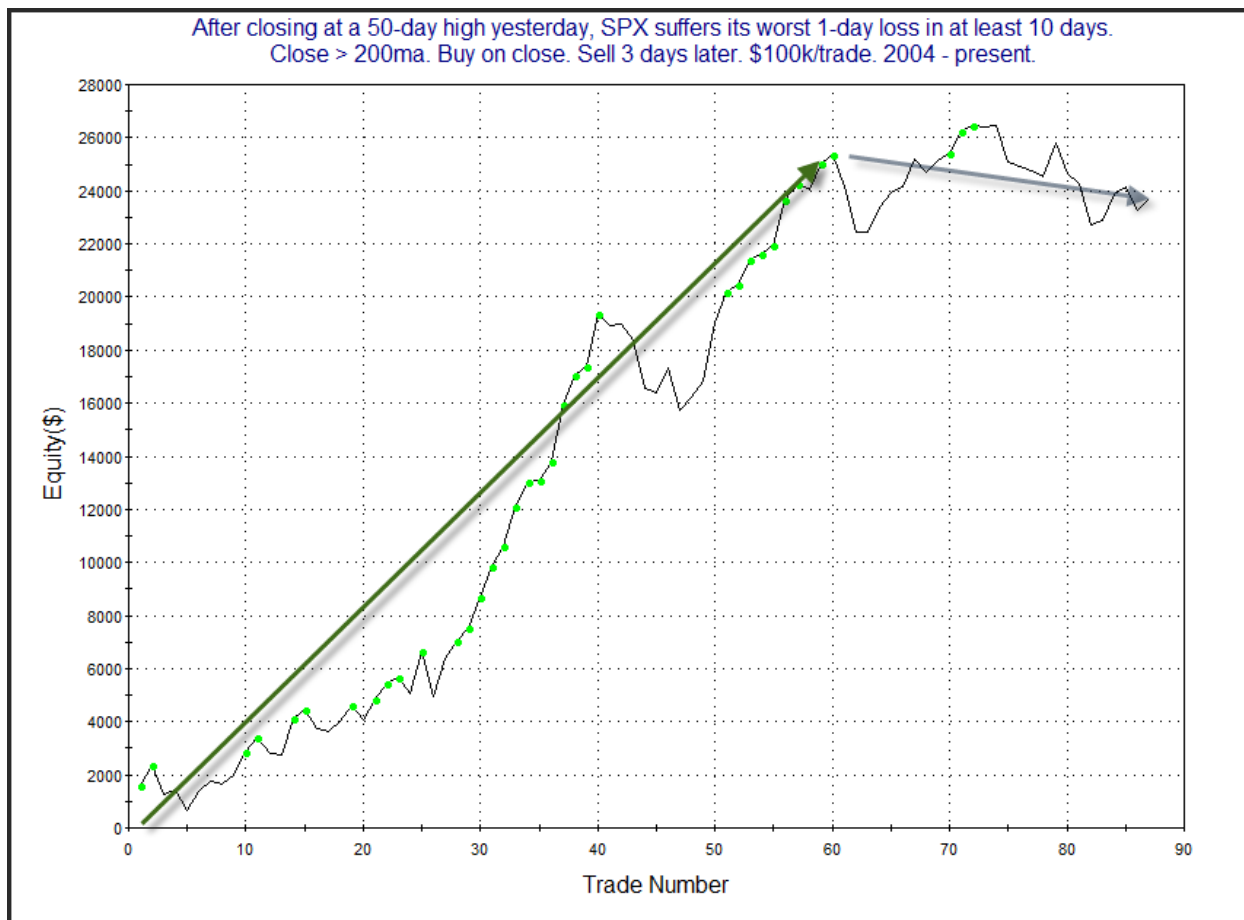
SPY posts an unfilled gap down after an unfilled gap up. Yesterday was the highest close in 20 days. Buy on close. Sell X days later. \$100k/trade. 1999 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Max Winning Trade	All: Max Losing Trade	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-23,019.58	38	18	20	47.37	1,827.28	-7,283.25	781.29	-1,854.14	0.42	0.38	-605.78
4	-17,262.64	38	16	22	42.11	1,998.36	-3,746.95	754.02	-1,333.04	0.57	0.41	-454.28
3	-14,483.74	38	16	22	42.11	1,044.24	-2,191.22	586.95	-1,085.23	0.54	0.39	-381.15
2	-11,218.83	39	14	25	35.90	1,383.20	-2,232.00	562.66	-763.85	0.74	0.41	-287.66
1	-7,783.27	39	15	24	38.46	1,008.68	-1,807.92	438.20	-598.18	0.73	0.46	-199.57

The numbers here appear to suggest a downside edge. Let's also take a look at a profit curve.



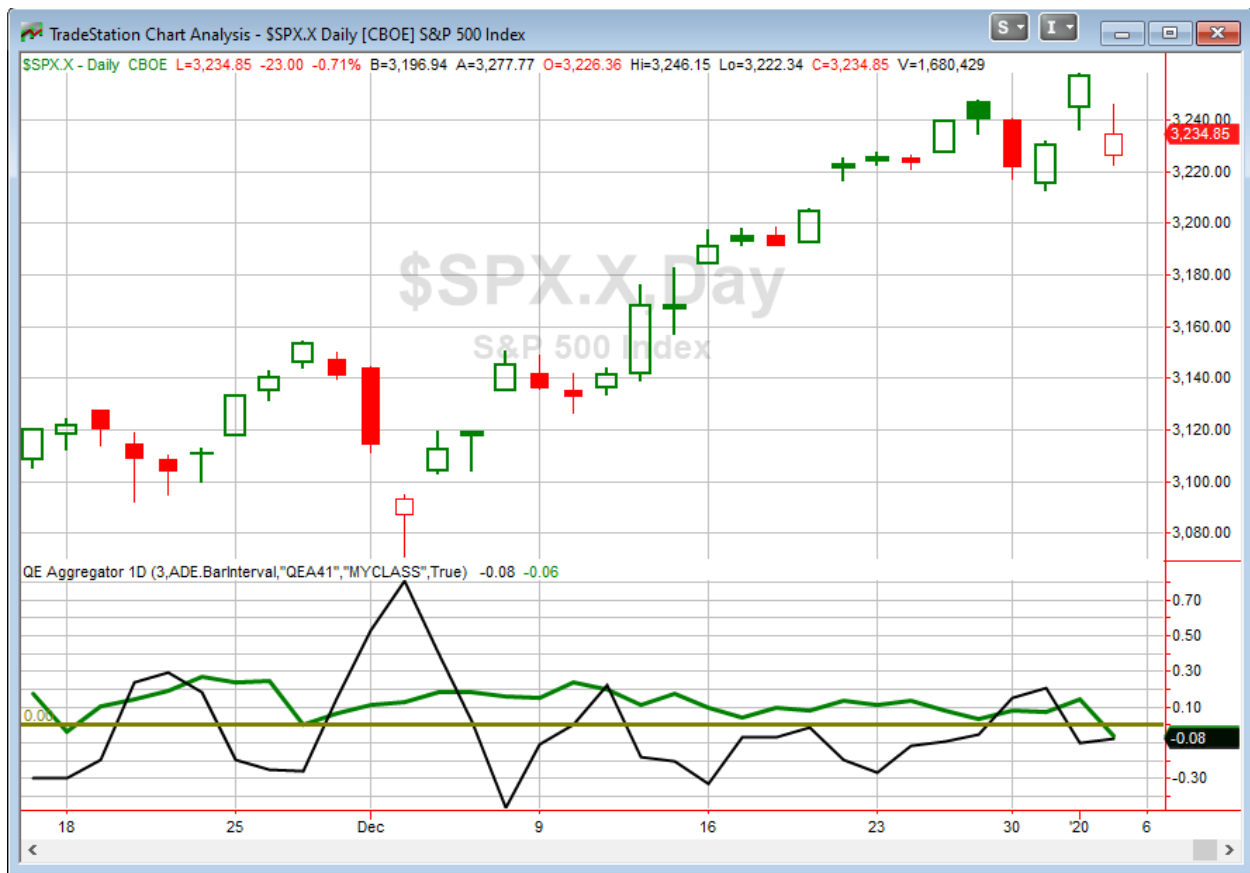
While the curve is choppy, it has persisted downwards. We have tracked this study for a while, and the edge has seen an acceleration to the downside in recent instances. This all suggests we could see further selling over the next few days. I added this to the Active List tonight.

The Quantifinder also noted a couple of studies suggesting possible bullish implications. But they simply have not played out in a bullish manner over the last few years. The one below looks at relatively big drops from a 50-day high. It had shown a bullish tendency in the following days for a while.



With basically the last 1/3 of the curve not exhibiting any edge, I am not inclined to include this on the Active Studies list. If it does not begin to reassert itself soon, I will remove it from the Quantifinder altogether. So I will just be adding the one bearish study tonight to the Active List.

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



With the new study considered, the green Aggregator Line dipped 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 list of active studies, expectations are slated to remain bearish on Monday. Of course this could change if compelling new bullish evidence emerges. Meanwhile, the Differential Pivot will be *inverted* at 3236.74 on Monday. That is about 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 is going to need to close up a couple of points if it is to remain "overbought" vs recent expectations. Anything other than that and it will flip to an "oversold" status on Monday's close.

So evidence is suggesting we could see a further decline in the coming days. The gap to a new high and then gap down from there has often seen more selling in the coming days. The study I discussed Thursday showed that the strong first trading day of January is often followed by a couple of more positive days, but then a possible swoon. And since there has not been a substantial

dip (a close below the 10ma) in either the SPX or NDX since early December, this run higher is starting to get overextended. So there are ample reasons to think we could see some selling in the next few days. But it is also worth considering the inverted Differential Pivot. I often view inverted pivots as opportune times to take profits on positions – *not* opportune times to enter new positions. This is because reward/risk is poor. Any move in the anticipated direction (down in this case) would mean the Differential flips and the (bearish) setup ends. A move against, though, does not have the same 1-day limitation. So reward is quite limited, but risk isn't. That in itself would keep me from looking at a short index position here. The fact that we are in the midst of a strong SOMA expansion in an intermediate-term bullish environment cements my lack interest. No point in trying to make a counter-trend trade with limited profit potential. I will continue to wait for a more favorable setup to emerge. And with the current geopolitical environment, we could easily see strong movements and overreactions leading to substantial short-term edges in the coming days and weeks.

***Intermediate-term Outlook (2 weeks – 2 months) – updated 1/6 – bullish***

<b>Combo #1</b>	<b>Combo #2</b>	<b>Combo #3</b>
<b>Long</b>	<b>Long</b>	<b>Long</b>

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 all 3 Combo Systems remained on long signals.*

Friday's selloff caused the major indices to finish mixed on the week. The SPX declined 0.2%, the NASDAQ rallied 0.2%, and the Russell 2000 declined 0.5%. SPX and NASDAQ again made new highs, so the trend remains up. There was one study featured in the Monday night letter that suggested bullish intermediate-term implications. I have copied it below.

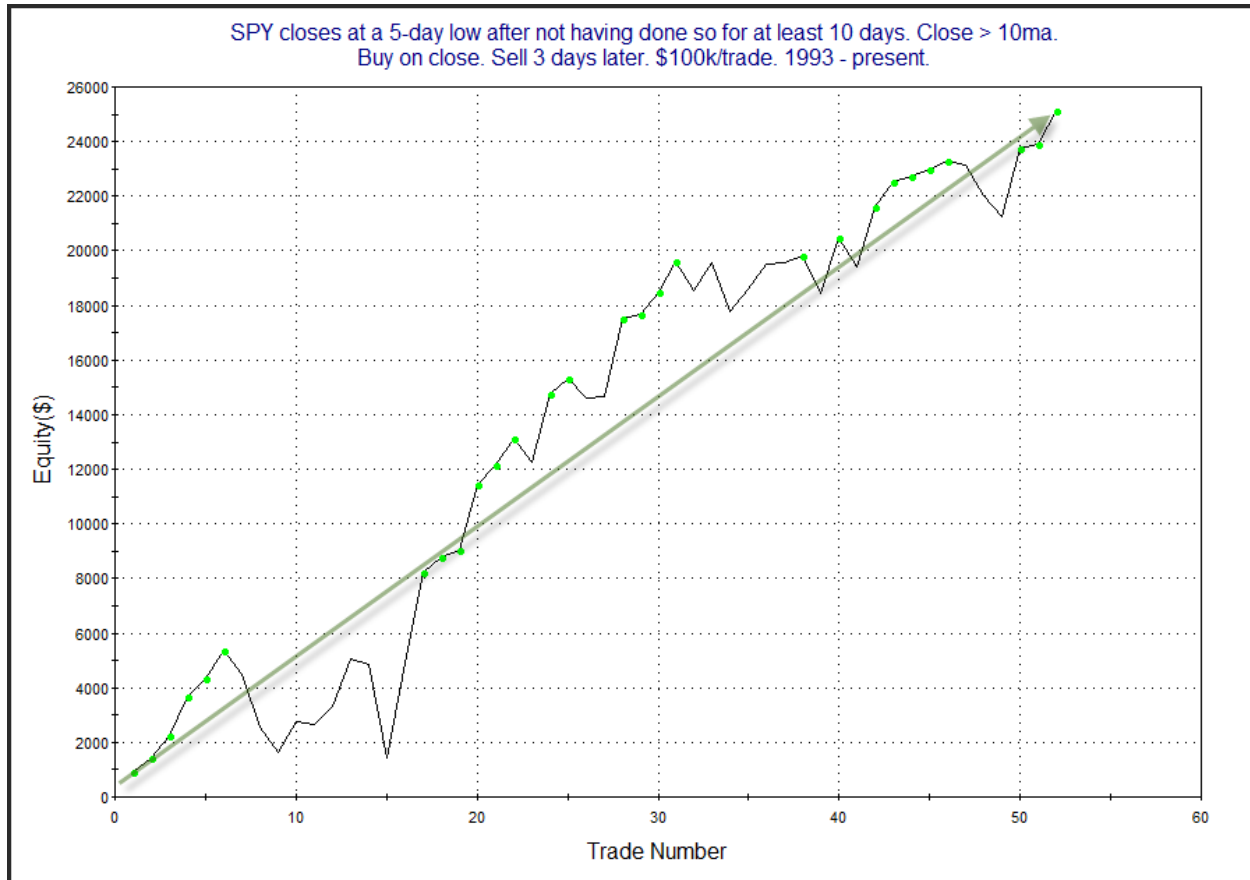
*Monday's action caused SPY to close in an interesting position. Traders could look at the chart and say it is "short-term oversold" due to the fact that it closed at a 5-day low. They might also say it is "short-term overbought" since it closed above its 10-day moving average. I have found that edges often arise when something is short-term overdone in one timeframe, but overdone in another direction in another timeframe. The study below looks at the current discrepancy. It was last seen in the 11/22/19 letter and has been updated.*

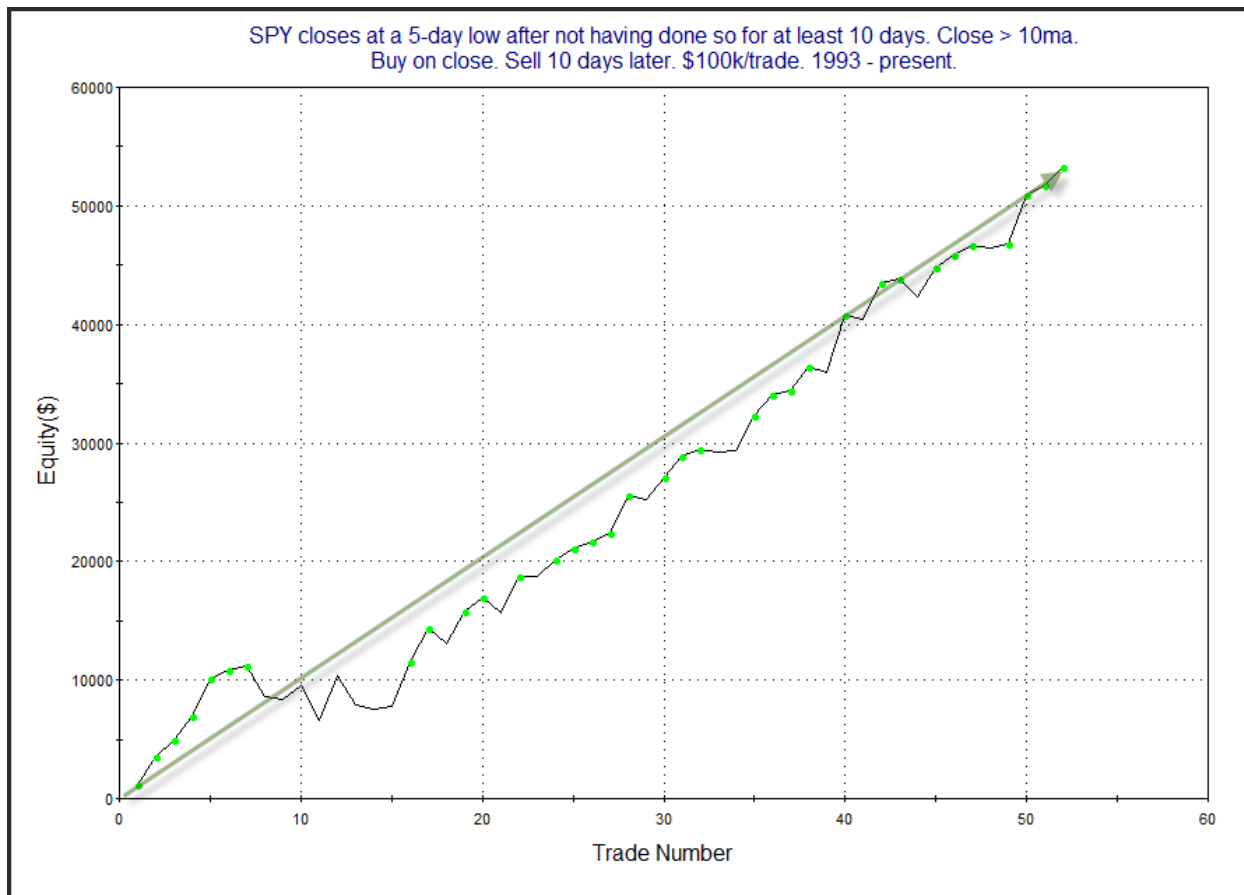
SPY closes at a 5-day low after not having done so for at least 10 days. Close > 10ma.  
Buy on close. Sell X days later. \$100k/trade. 1993 - present.

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	53,244.78	52	38	14	73.08	4,839.66	-2,972.16	1,782.73	-1,035.64	1.72	4.67	1,023.94
9	46,739.63	52	39	13	75.00	5,293.08	-3,319.71	1,618.02	-1,258.71	1.29	3.86	898.84
8	42,571.51	52	39	13	75.00	4,734.72	-2,602.71	1,489.34	-1,193.29	1.25	3.74	818.68
7	37,656.60	52	37	15	71.15	4,118.22	-3,472.29	1,551.42	-1,316.38	1.18	2.91	724.17
6	33,504.44	52	34	18	65.38	4,307.28	-2,992.38	1,472.72	-920.44	1.60	3.02	644.32
5	32,256.05	52	34	18	65.38	4,496.34	-3,570.00	1,423.96	-897.69	1.59	3.00	620.31
4	28,259.04	52	34	18	65.38	3,240.45	-2,475.20	1,293.71	-873.72	1.48	2.80	543.44
3	25,109.01	52	37	15	71.15	3,452.40	-3,393.78	1,120.15	-1,089.11	1.03	2.54	482.87
2	14,971.34	52	33	19	63.46	3,809.72	-3,737.28	973.94	-903.62	1.08	1.87	287.91
1	7,025.17	52	29	23	55.77	2,225.48	-3,909.03	735.01	-621.31	1.18	1.49	135.10

**47 of 52 instances (90%) closed above the entry price at some point in the next week.**

Results here suggest a solid edge over the next 1-10 days. And nearly half of the gains have been realized in just the 1st 3 days. Below are profit curves for both the 3 and 10-day timeframes.



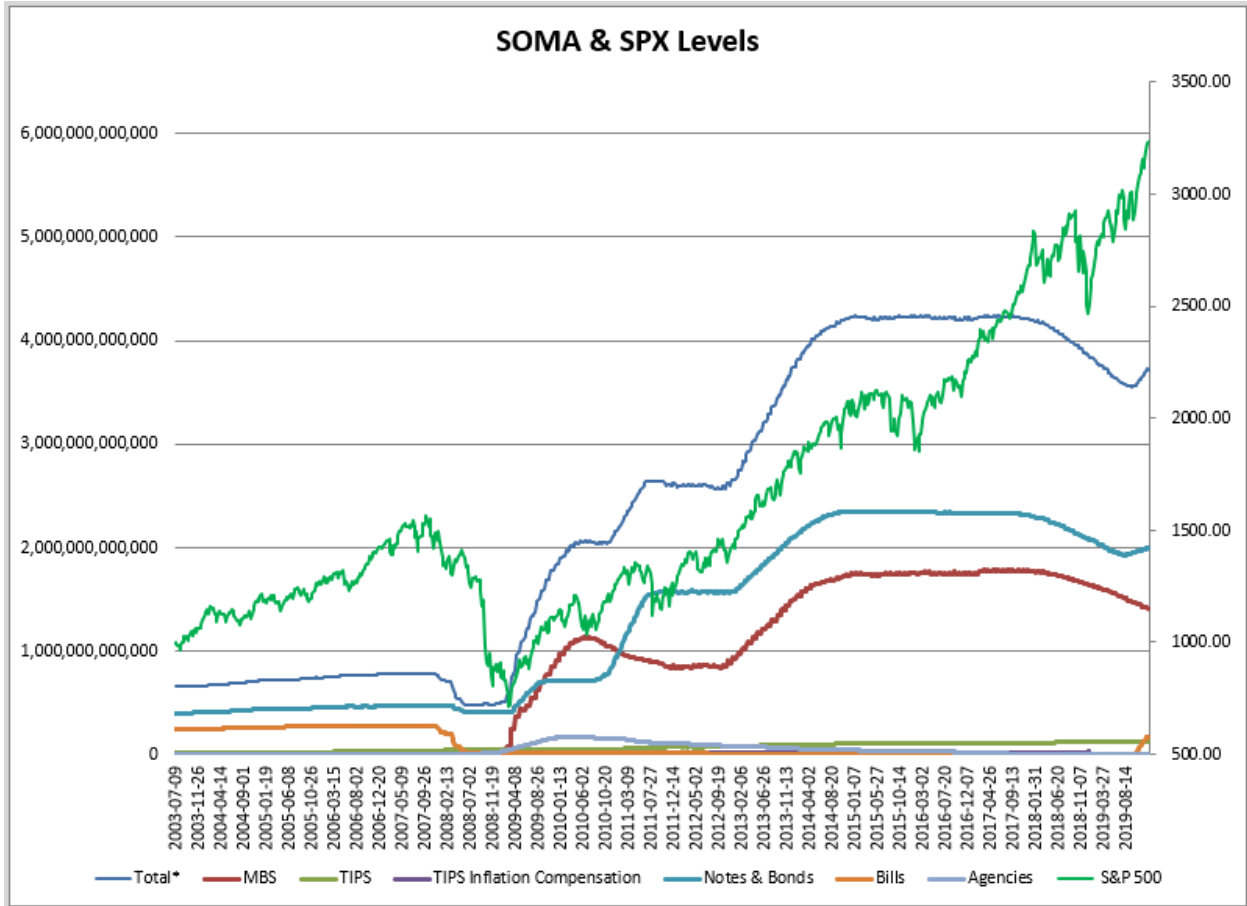


*The strong, steady upslopes are impressive and serve as some confirmation of the bullish edge. I have added this study to both the short-term and intermediate-term active lists.*

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.*

*The Quantitative Tightening program that began in October 2017 was ended in August 2019. In October 2019 a new Fed policy, nicknamed “not QE” was put in place and it has generated further SOMA expansion.*



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

« As of 12/24/2019

DOMESTIC SECURITIES HOLDINGS AS OF  
**December 31, 2019**

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

Security Type	Total (in Thousands)
US Treasury Bills (T-Bills)	169,525,000.0
US Treasury Notes and Bonds (Notes/Bonds)	1,989,140,922.2
US Treasury Floating Rate Notes (FRN)	17,408,716.4
US Treasury Inflation-Protected Securities (TIPS)*	127,384,337.6
Federal Agency Securities**	2,347,000.0
Agency Mortgage-Backed Securities***	1,408,676,620.6
Total SOMA Holdings	3,714,482,596.8
Change From Prior Week	-11,303,544.7

\*Does not reflect inflation compensation of 25,474,316.4

\*\*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 01/02/2020 4:30pm.

The SOMA declined \$11.3 billion this past week. This is the first week it has not risen at least \$5 billion since “not QE” began 11 weeks ago. And since “not QE” has been in effect, SPX has closed higher 10 of those 11 weeks and gained over 8.1% in total. Like past QE policies, “not QE” certainly seems to be favorable for the market. Betting against the market when there is a substantial SOMA expansion underway has never been a good idea.

The intermediate-term active list is still dominated by bullish studies. The SPX & NASDAQ are near all-time highs. The new study this past week also appears to be a positive. Both the Best 6 Months and the Presidential Cycle are bullish. This means all 4 Market Timing Course indicators remain bullish. And the recent SOMA expansion seems to be having the same type of positive market impact that past SOMA expansions did. Overall, the bullish case seems substantially stronger. I remain bullish on the intermediate-term. I will therefore keep a generally more aggressive approach with long trades and a very conservative approach when considering short trades.

## **Catapult and Capitulative Breadth Statistics**

[Catapult & CBI Presentation Link](#)

### ***OpenCatapult Triggers***

*New*

TGT – 1/3 @ \$124.76 (buy @ LIMIT)

### ***Broad Market Large Cap CBI – 1(TGT)***

### **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.*

**TGT – Buy 1/3 Catapult position @ \$124.76 LIMIT.** From the Catapult section above, this is the 1<sup>st</sup> of up to 3 possible lots of TGT.

### **Current Open Trade Ideas**

*None*

*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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