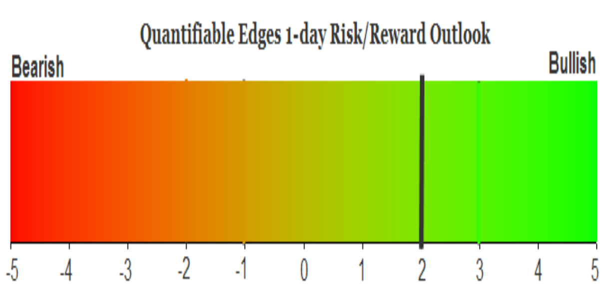
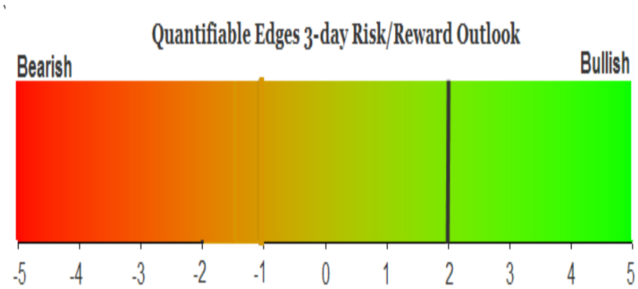
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 4, 2020 Volume 13 Issue 173

Market Overview





Signals Overview

Aggregator	CBI Reading
Long	0

Tonight's Research Points

- Coming from an intermediate-term high, an unfilled gap down after an unfilled gap up appears to be somewhat bearish.
- Big down days bounce more reliably if the follow a short-term low than if the originate after a short-term high.
- The VIX spike suggests a 1-day bounce.
- The 1st close below the 10ma after 25+ days above it is often buyable.

Short-term Outlook
The Bottom Line

The Aggregator bullish. While the selling could have further to go, I believe the upside edge is strong enough that I will look to start building a long index position.

The Evidence

Big selling Thursday. The SPX lost 3.5%, the NASDAQ tumbled 5.0%, and the Russell 2000 fell 3.0%. Breadth was negative as the NYSE Up Issues % was 20% and the Up Volume % came in at 26%. NYSE total volume rose from Wednesday's level.

The "wonky" action I discussed last night had me concerned, but I did not think it would result in the largest ever drops from an all-time high the very next day. But that is what happened. Now if you use the S&P 90 predecessor index when looking back, you'll see that on 9/26/55 there was a 6.6% decline from an all-time high. And on 11/15/91 the SPX decline 3.9% after making an all-time intraday high on 11/14/91, but closing down slightly on day and just missing an all-time high close. For the NDX (-5.23%) it was the 2^{nd} largest decline from a 1-year high, trailing only 1/4/2000 (-6.45%). On 6/11/20 the NDX did close down 5.01%, which was the only other drop greater than 5%.

Big down days can be signs of a washout. But that is much less likely when the big selloff originates from a high are than it does from a low are. This is something I have discussed numerous times in the past. Additionally, it generally helps if there is not a sizable move of the intraday low on these big downs days. Thursday did not bounce greatly from the low before the close, but it did originate from a high. The studies below are from 8/6/19 and 11/10/11 letters. They demonstrate the impact of strong selling from a high vs a low. Stats are all updated.

After closing at a 5-day ***low*** yesterday, SPY closes down over 3% today and within 1% of its intraday low. 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
5	84,786.06	30	23	7	76.67	19,398.00	-12,514.32	4,698.43	-3,325.40	1.41	4.64	2,826.20
4	59,343.76	32	20	12	62.50	17,914.00	-8,109.60	4,519.07	-2,586.47	1.75	2.91	1,854.49
3	36,432.95	33	19	14	57.58	14,708.85	-11,518.47	4,164.48	-3,049.45	1.37	1.85	1,104.03
2	60,428.74	34	27	7	79.41	12,693.50	-9,320.67	3,203.82	-3,724.91	0.86	3.32	1,777.32
1	52,333.47	35	24	11	68.57	11,683.71	-4,080.40	3,032.19	-1,858.10	1.63	3.56	1,495.24

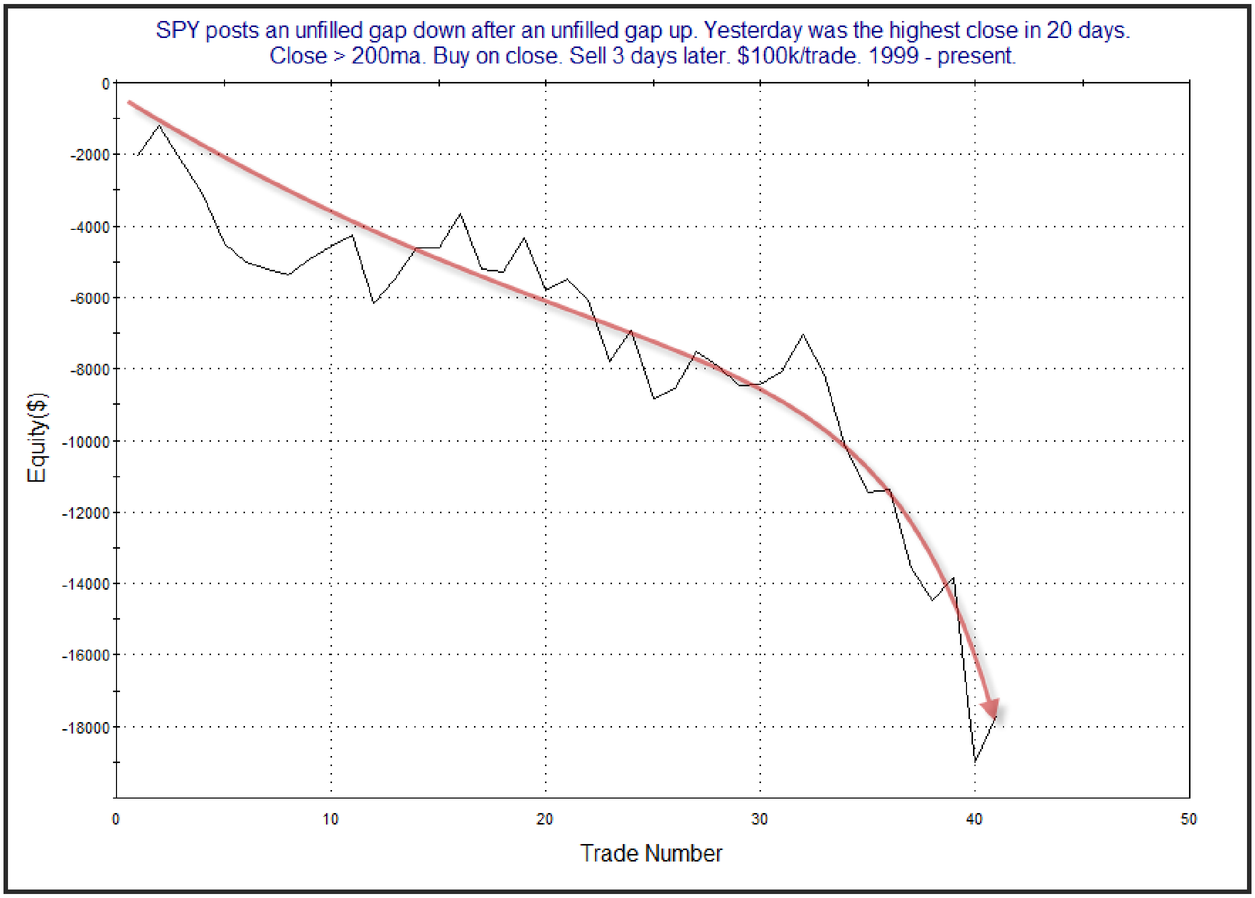
After closing at a 5-day ***high*** yesterday, SPY closes down over 3% today and within 1% of its intraday low. Buy on close. Sell X days later. $100k/trade. 1993 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Max Winning Trade	All: Max Losing Trade	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-12,511.52	12	5	7	41.67	10,819.13	-17,935.50	3,563.35	-4,332.61	0.82	0.59	-1,042.63
4	-3,461.07	12	5	7	41.67	7,082.94	-9,273.00	3,293.57	-2,846.99	1.16	0.83	-288.42
3	2,948.39	12	7	5	58.33	3,882.23	-4,633.20	1,852.74	-2,004.16	0.92	1.29	245.70
2	3,497.18	12	8	4	66.67	6,340.57	-9,315.90	2,233.72	-3,593.15	0.62	1.24	291.43
1	3,236.93	12	7	5	58.33	3,845.72	-2,033.04	1,424.02	-1,346.24	1.06	1.48	269.74

With the 2nd of these studies triggering on Thursday, the pattern does not appear bullish like it would if the selling came right after a 5-day low.

Another study appeared that suggested the action the last couple of days could lead to more selling. This study 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 7/17/20 Subscriber Letter. Below are updated results.

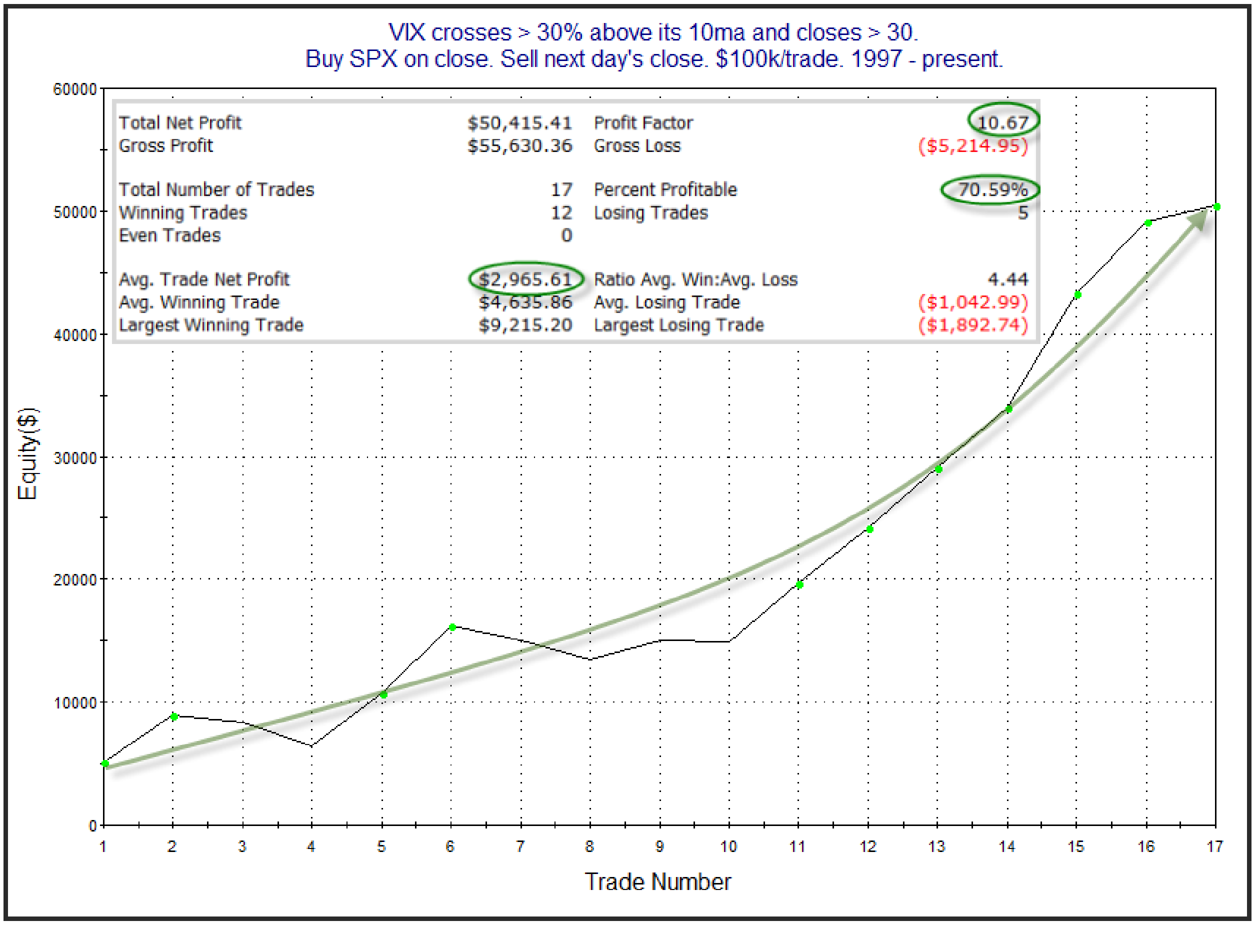
SPY posts an unfilled gap down after an unfilled gap up. Yesterday was the highest close in 20 days. Close > 200ma. Buy on close. Sell X days later. $100k/trade. 1999 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Max Winning Trade	All: Max Losing Trade	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-23,756.84	41	20	21	48.78	1,827.28	-7,283.25	788.06	-1,881.81	0.42	0.40	-579.44
4	-18,333.61	41	18	23	43.90	1,998.36	-4,273.14	848.14	-1,460.87	0.58	0.45	-447.16
3	-17,695.30	41	18	23	43.90	1,312.42	-5,156.38	629.78	-1,262.23	0.50	0.39	-431.59
2	-16,297.78	42	16	26	38.10	1,383.20	-6,275.98	567.15	-975.85	0.58	0.36	-388.04
1	-7,669.43	42	17	25	40.48	1,008.68	-1,807.92	426.09	-596.52	0.71	0.49	-182.61

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



While the curve is a little 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.

But not everything was bearish. Also notable was the action in the VIX, which rose 26.5% on Thursday. An interesting study from the Quantifinder was from the 8/5/11 letter. It notes not only that the VIX is relatively stretched on a short-term basis, but that the VIX reading is also somewhat high on an absolute basis. Over the years I have found that short-term stretches are not as impactful when the stretch is coming from a very low level. This is the reason the VIX > 30 is also included as a filter. Results are updated.



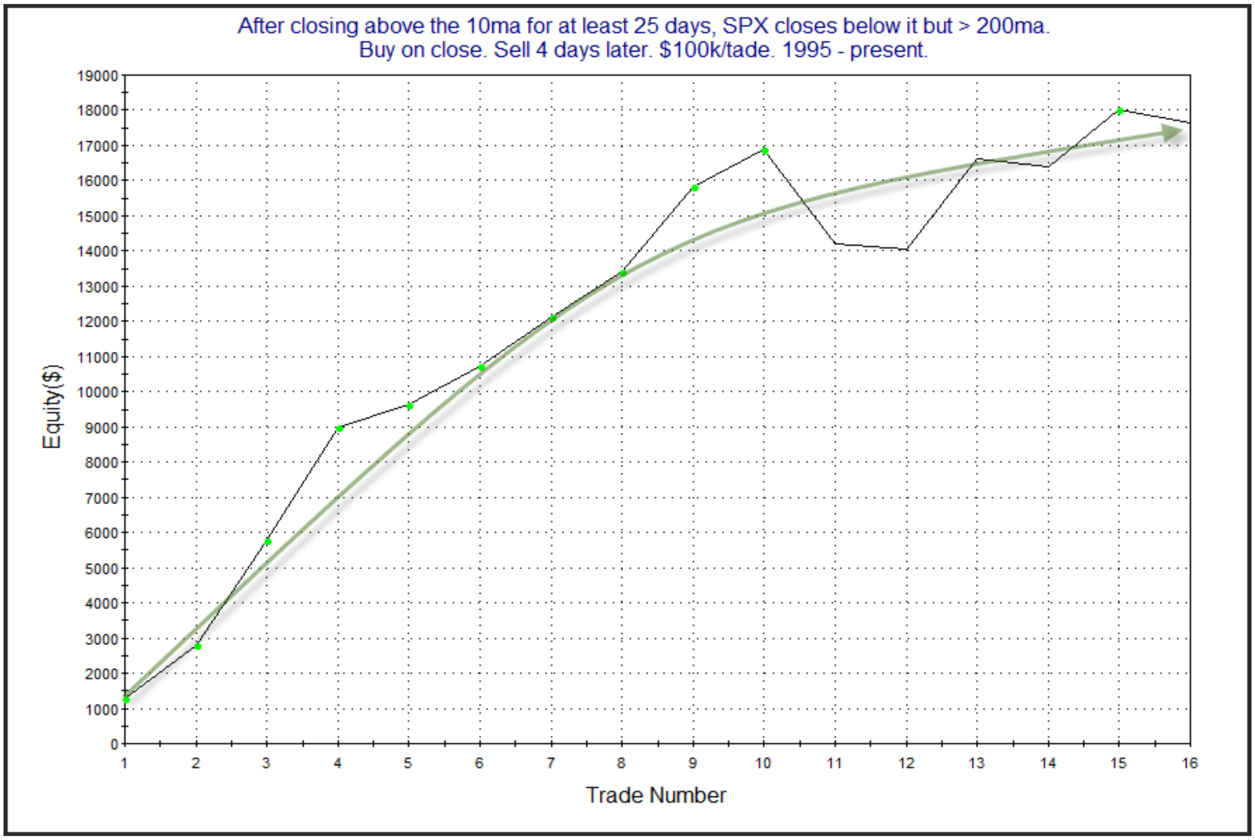
Instances are a little lower than I'd prefer, but the stats are very strong, and the curve is fairly smooth. The average performance the day after the setup has been a 3% gain. That is a huge average for just a 1-day trade.

The persistent uptrend of late has kept SPX above its short-term moving averages for an extended period. Tuesday, after 26 consecutive closes above the 10ma, SPX sliced down and closed below it. In the 4/6/16 letter I looked at performance following other instances where SPX closed below its 10ma for the first time over 25 days. Results are updated below.

After closing above the 10ma for at least 25 days, SPX closes below it but > 200ma.
Buy on close. Sell X days later. $100k/tade. 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	30,584.69	16	14	2	87.50	5,825.05	-3,062.88	2,435.65	-1,757.20	1.39	9.70	1,911.54
9	30,500.35	16	15	1	93.75	6,462.89	-2,453.28	2,196.91	-2,453.28	0.90	13.43	1,906.27
8	27,554.32	16	14	2	87.50	6,404.58	-869.28	2,034.82	-466.60	4.36	30.53	1,722.14
7	21,608.88	16	13	3	81.25	6,326.04	-1,310.40	1,842.23	-780.05	2.36	10.23	1,350.55
6	18,943.73	16	13	3	81.25	5,157.46	-1,396.50	1,692.05	-1,017.66	1.66	7.20	1,183.98
5	17,521.62	16	13	3	81.25	3,505.74	-2,098.50	1,616.19	-1,162.94	1.39	6.02	1,095.10
4	17,651.45	16	12	4	75.00	3,206.40	-2,665.92	1,753.88	-848.78	2.07	6.20	1,103.22
3	11,773.10	16	13	3	81.25	2,805.12	-1,630.30	1,202.23	-1,285.29	0.94	4.05	735.82
2	8,396.44	16	10	6	62.50	2,130.10	-1,425.20	1,099.89	-433.73	2.54	4.23	524.78
1	4,192.17	16	11	5	68.75	1,975.68	-1,555.20	595.86	-472.46	1.26	2.77	262.01

The numbers here all look solidly bullish. Below is a look at the 4-day profit curve.



We have seen a little bit of a fade lately, but this study still appears to be worth consideration.

I have updated the Aggregator chart below.

With tonight's mix of studies considered, 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 shot 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. Therefore, the Aggregator signal turned long at the close.

Based on the current list of active studies, expectations are set to remain positive on Friday. Of course, this could change if compelling new bearish evidence emerges. Meanwhile, the Differential Pivot will be 3537.35 on Friday. That is a whopping 2.4% above Thursday's close. Therefore, SPX would need to a very large 2.4% on Friday in order to flip from oversold to overbought vs recent expectations.

So the Aggregator is bullish. And evidence is leaning positive, though it is mixed. The fact that we sold off so strongly from a top, and with an unfilled gap down, could mean more selling in the coming days. The market can do anything, and the record drop from all-time highs is just another example of that. Employment numbers are set to be released on Friday morning at 8:30am, and they are capable of generating a sizable reaction. So that is another wildcard to consider. But I do think there is a bit of an upside edge here. So I will look to take on a partial index position on Friday if I can get a favorable entry price either at the open or the close. (I am not interested in buying into a selloff mid-day if that occurs after decent start to the day.) If the selling worsens on Friday, then I will likely continue to scale in after the weekend.

Intermediate-term Outlook (2 weeks – 2 months) – updated 8/31 – slightly bullish

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.

SPY – Buy ¼ index position @ $342.00 LIMIT ON OPEN. If not filled at the open, I will cancel my order and look to instead buy @ $342.00 LIMIT ON CLOSE. Based on the short-term outlook above, I a looking to start building a long index position.

Current Open Trade Ideas

None